U.S. Dept. of the Treasury

PRESS RELEASES

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE January 3, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $5,803 million of 13-week bills and for $5,801 million of 26-week bills, both to be issued on January 6, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing April 7, 1983			:	26-week bills maturing July 7, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	98.018 a/	7.841%	8.11%	:	95.996	7.920%	8.36%
Low	97.996	7.928%	8.20%	:	95.976	7.960%	8.41%
Average	98.004	7.896%	8.17%	:	95.983	7.946% 2/	8.39%

a/ Excepting 1 tender of $405,000.

Tenders at the low price for the 13-week bills were allotted 34%.
Tenders at the low price for the 26-week bills were allotted 47%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 52,095	$ 51,345	:	$ 76,940	$ 47,130
New York	10,940,960	4,365,960	:	11,802,925	4,298,135
Philadelphia	23,965	23,965	:	13,935	13,935
Cleveland	34,400	34,400	:	30,190	30,190
Richmond	40,500	40,500	:	25,045	25,045
Atlanta	35,295	35,295	:	29,230	29,230
Chicago	1,035,525	473,690	:	723,780	191,120
St. Louis	46,035	38,465	:	41,550	31,800
Minneapolis	24,310	16,310	:	24,215	19,215
Kansas City	43,915	41,225	:	37,645	36,645
Dallas	32,110	27,110	:	16,295	16,295
San Francisco	838,110	373,510	:	1,323,305	760,685
Treasury	281,075	281,075	:	301,375	301,375
TOTALS	$13,428,295	$5,802,850	:	$14,446,430	$5,800,800
Type					
Competitive	$11,341,925	$3,816,480	:	$12,200,265	$3,654,635
Noncompetitive	913,960	913,960	:	703,765	703,765
Subtotal, Public	$12,255,885	$4,730,440	:	$12,904,030	$4,358,400
Federal Reserve	1,012,110	912,110	:	1,000,000	900,000
Foreign Official Institutions	160,300	160,300	:	542,400	542,400
TOTALS	$13,428,295	$5,802,850	:	$14,446,430	$5,800,800

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 8.076%.

R-1090

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. January 4, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $11,600 million, to be issued January 13, 1983. This offering will provide $625 million of new cash for the Treasury, as the maturing bills are outstanding in the amount of $10,983 million, including $1,224 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and $2,251 million currently held by Federal Reserve Banks for their own account. The two series offered are as follows:

91-day bills (to maturity date) for approximately $5,800 million, representing an additional amount of bills dated October 14, 1982, and to mature April 14, 1983 (CUSIP No. 912794 CR 3), currently outstanding in the amount of $5,626 million, the additional and original bills to be freely interchangeable.

182-day bills (to maturity date) for approximately $5,800 million, representing an additional amount of bills dated July 15, 1982, and to mature July 14, 1983 (CUSIP No. 912794 DA 9), currently outstanding in the amount of $6,034 million, the additional and original bills to be freely interchangeable.

Both series of bills will be issued for cash and in exchange for Treasury bills maturing January 13, 1983. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, January 10, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on January 13, 1983, in cash or other immediately-available funds or in Treasury bills maturing January 13, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS
epartment of the Treasury • Washington, D.C. • Telephone 566-204

FOR IMMEDIATE RELEASE
January 7, 1983

CONTACT: Robert Don Levine
(202) 566-2041

Chrysler Loan Guarantee Board Approves UAW Contracts

The Chrysler Loan Guarantee Board announced today it has unanimously approved by notational vote the labor contracts with the Chrysler Corporation ratified last month by the American and Canadian United Auto Workers unions.

Secretary of the Treasury Donald T. Regan is chairman of the Board. The other voting members are Chairman of the Federal Reserve Board Paul A. Volcker and Charles A. Bowsher, Comptroller General of the United States.

R-1092

TREASURY NEWS

epartment of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE January 10, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $ 5,801 million of 13-week bills and for $ 5,801 million of 26-week bills, both to be issued on January 13, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing April 14, 1983			:	26-week bills maturing July 14, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	98.066	7.651%	7.91%	:	96.082 a/	7.750%	8.18%
Low	98.054	7.698%	7.96%	:	96.063	7.787%	8.22%
Average	98.061	7.671%	7.93%	:	96.070	7.774% 2/	8.20%

a/ Excepting 1 tender of $100,000.

Tenders at the low price for the 13-week bills were allotted 19%.
Tenders at the low price for the 26-week bills were allotted 69%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 58,340	$ 58,340	:	$ 80,740	$ 40,740
New York	13,126,210	4,271,730	:	12,070,060	4,549,955
Philadelphia	16,330	16,330	:	67,400	17,400
Cleveland	67,870	34,870	:	50,150	25,150
Richmond	59,450	42,540	:	38,415	33,415
Atlanta	49,770	48,830	:	36,385	33,785
Chicago	1,081,795	99,795	:	954,560	193,460
St. Louis	53,415	43,415	:	56,005	40,005
Minneapolis	15,010	10,430	:	16,495	13,475
Kansas City	46,315	46,315	:	50,155	41,755
Dallas	30,315	30,315	:	18,815	13,815
San Francisco	1,160,185	799,465	:	1,246,860	439,240
Treasury	298,520	298,520	:	359,130	359,130
TOTALS	$16,063,525	$5,800,895	:	$15,045,170	$5,801,325
Type					
Competitive	$13,638,495	$3,375,865	:	$12,375,175	$3,131,330
Noncompetitive	994,795	994,795	:	825,395	825,395
Subtotal, Public	$14,633,290	$4,370,660	:	$13,200,570	$3,956,725
Federal Reserve	1,126,435	1,126,435	:	1,125,000	1,125,000
Foreign Official Institutions	303,800	303,800	:	719,600	719,600
TOTALS	$16,063,525	$5,800,895	:	$15,045,170	$5,801,325

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 7.968%.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

EMBARGOED FOR RELEASE UPON DELIVERY
Expected at 1:30 p.m.
Wednesday, January 12, 1983

Remarks
by
Donald T. Regan
Secretary of the Treasury
before the
Washington Post
Annual Business Luncheon
Washington, D.C.

There are probably 100 good speech themes I could elaborate on this afternoon. But there is only one that anybody in this town cares about these days: the budget. I am sure you all followed the news of the last week -- the forecasts, the deficits, the Congressional leaders flowing in and out of the White House and all of the economic scenarios that came with them.

It reminds me of the story about the surgeon, the engineer and the economist who found themselves together at the gates of Heaven. They were arguing about whose profession in life was the oldest.

"It's mine" said the surgeon, "because the Bible said that God created man and then woman from one of Adam's ribs and that is clearly a surgical operation."

But the engineer said before God created man, he created the world out of chaos and that was an engineering job.

At that point the economist looked calmly at both of them and said, "Yes, but who do you think created the chaos?"

Although you have already heard some pretty specific budget stories, I cannot give too many details. But I can and will talk about the central issues and the hard choices that must be made.

It is clear that we are in for several months of intense debate and discussion on the budget and spending. And the side of the discussion you support will be largely determined by your preconceived frame of reference. For many, that frame of reference has become seriously distorted in two important ways.

The first problem has to do with the whole idea of spending and spending increases.

R-1094

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, February 28, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on March 3, 1983, in cash or other immediately-available funds or in Treasury bills maturing March 3, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

As defense spending was going down as a portion of the budget, what was happening to outlays for social programs? There has not onl been a steady increase; but in the past several years that increasing trend has become an exploding upward spiral. Spending for human resources -- such categories as education, training, health, income security and the like -- increased from $25 billion in 1960 to $72 billion in 1970 and to over $300 billion in 1980. Now, these same figures as a percentage of the total budget, went from 28 percent to 37 percent to 52 percent in 1980. And in 1981 that category of spending went up further to over 345 billion or almost 53 percent of total spending.

Spending for human resources was over $372 billion in the fiscal year just ended. And based on last year's estimates, will grow to $386 billion in the current fiscal year and to over $400 billion next year. And yet we still hear that the Administration is cutting back on social programs!

Now with the explosive increase in total government spending, the portion of the budget that must by syphoned off each year to service that debt has also gone up. From 1955 through 1975, the percentage o the budget needed to service the debt was about 7%. The percentage went up to 9% in 1980. In FY 81, it increased further to 10.5 percent and this year it was a staggering $85 billion or 11.6 percent of the budget.

If you really stop to consider the dimensions of all this, it kin of boggles the mind. But we don't stop to consider it very often. Sadly, these trends and big numbers are nothing new. And, as a nation, we are getting a little numb to it all.

But whether we are talking about a billion dollars or a nickel -- it is money that has been hard earned by the American people and that must come one way or another out of the pockets of the American people.

Now in addition to calling spending increases something other tha what they are, we have concocted a second way to confuse the spending issue.

Some years ago the word 'uncontrollable' crept into the debate about spending and the budget. It is a term typically applied to the social spending side of the budget: items such as Social Security, Medicare, Medicaid, student loans and the like. Once such a program is signed into law, so goes the argument, the outlay of funds flows "automatically." The concept of an uncontrollable expenditure is applied also -- although usually to a lesser extent -- to defense spending. The idea here, of course, is that the process of procuring a weapons system involves a long, multi-year process of research and development, testing, redesign, and production. And, of course, once into production, the economies of scale often require that a large number of the systems be built so that the price per unit can be reduced. Persuasive arguments are usually made that once we are part way through a weapons system procurement it is often unwise to then stop in mid-stream.

What we have then -- both in the case of domestic transfer payments and defense spending, is a series of very powerful institutional and procedural factors which make it very difficult to halt or slow a Federal spending program once it has been put into place.

But what is our response to this situation? Do we simply throw u our hands and say "the budget is uncontrollable."? Have we put into motion a spending machine whose momentum is so great that the creator of that machine are now powerless to reign it in? I reject that notion.

We are a free people with a freely elected legislative body and a elected president. If we as a nation do not have control over our ow budget, what do we have control of? Many are on the verge of abdicating the overall levels of expenditures to forces which they themselves set in motion. If we do this, where are we headed?

What I am suggesting is that that we as a national community have the power -- if we choose to use it -- to control spending.

We in the Reagan Administration have said repeatedly that we are going to honor the basic commitment of the Federal Government to thos truly in need. And, contrary to much of the scare talk that was hear before the election last fall, social security beneficiaries are goin to receive their checks, and they will not be reduced from their current levels. At the same time, however, it is obvious to anyone who does not have their head completely in the sand that the Social Security system as it is now constituted cannnot continue indefinetly The system is currently paying out about $30,000 dollars more each minute than it is taking in. Nothing can go on indefintely like that There is no company which can stay in business nor any individual which can make ends meet, on that basis. And, wishful thinking not withstanding, there is no government program -- in the world -- which can function indefinitely on that basis.

Now in talking about spending there is always the inflation factc to contend with. It looks as though inflation for this calendar yeai will be somewhere in the 4-5% percent range. So when we start talkir about the Administration's proposed Fiscal year 1984 budget let's bea in mind some simple rules of thumb. If the budget level for a particular agency, program or category is less than that for the last fiscal year, that is a budget cut. If it grows by a factor of 4% or less that is a slight increase in nominal terms and -- depending on the figure -- about the same or a slight decrease in real terms. Any figure that is more than 5% greater than last year's figure is an increase both in real and nominal terms. It is not a slash. It is not being tightfisted to the point of insensitivity. It is not a reduction. It is an increase. Period.

Other nations are learning that they cannot spend their way to prosperity. Debts must all be repaid -- eventually. Living on credi where each year debt servicing constitutes a greater slice of nationa earnings is not a national lifestyle that can go on forever. Uncle Sam has been very adament in making sure that point is driven home to other nations. And it is well that we do so. But we had better lear the lesson ourselves. We cannot afford to keep saying, "Do as I say and not as I do."

Future deficits are going to be large and they are worrisome. But they have not grown larger only -- I might say, not even primarily -- because of the tax cuts. In spite of the cut and in spite of the recession, "government receipts", taxes by another name, have actuall gone up -- from $599 billion in 1981 to $618 billion in 1982. This year's revenues will be about $600 billion, a reduction. But while government revenue was going up, spending was going up more by almost $70 billion. The underlying cause of these deficits is really two-fold. First, the recession has reduced personal and business income and therefore reduced tax receipts. And that is why the President rightly pointed out last week in his press conference that getting an economic recovery is an essential ingredient in reducing the deficits. But the other cause stems, of course, from decades of overspending -- which are also, by the way contributing causes to the slow economic growth.

We need to view all of this in terms of the gross national product.

This Administration came into office committed to reducing spending as a percentage of GNP. Unfortunately, that percentage has gone up, not down.

But that is still an over-riding goal. Spending must be brought down to 21 to 22 percent of GNP by 1986. If we are serious about thi -- and we are -- no program should be automatically immune from cuts.

Now while we are bringing outlays down, we have to start bringin revenues up to meet the outlays.

Obviously, more revenue can best be raised from a growing base. To enable that base to expand several favorable conditions must be present.

First, interest rates, which have dropped substantially, are still too high. There are many economists who will tell you that there is no technical correlation between deficits and interest rates. And as an academic point, there may be some truth here. But as a man who worked on Wall Street for thirty five years, I can tell you that there is a powerful perception in the marketplace that massive deficits will bring on rising interest rates. And that perception has a way of becoming a self fulfilling prophesy. That is why spending must move down and revenues up, respectively, into that range of 21-22 percent of GNP.

In my judgement, interest rates in the long run will move down further and stay down only if we get deficits below 2% of GNP.

Secondly, to ensure that we can look forward -- in the near term - to an expanding economic base, monetary policy should be accommodative to recovery. Then, as the economy strengthens, money growth should be phased back slowly.

Finally, if we want to strengthen an expanding economic base, increased attention must be paid to streamlining and simplifying the federal tax structure. We have a tax code in this country that has more than a thousand pages. It is only the well-to-do who can afford the lawyers and accountants needed to really pore over the whole matrix. I recognize that any really serious attempt to reform that code will bring out the special interest groups like flowers bring bees. All will be trying to maintain 'their' special circumstances or 'their' loophole.

But it is high time that interest groups thought more in plural terms and less in singular. Remember that the U.S., in lower case, is "us" and that is who should be considered. An excessive preoccupation with "I" or "our group" or "my interest" is simply not compatible with fiscal responsibility, nor with simplfying the tax system.

To reach all these goals we will need a lot of honest and serious dialogue on the real issues; not bamboozling rhetoric.

The question which faces the United States and many other nations in the world is: What overall levels of public sector spending and public sector revenues will maximize the prospects of vigorous economic recovery? This Administration is determined to identify those levels and work cooperatively with Congress to stay within them.

Thank you.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. January 11, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $12,000 million, to be issued January 20, 1983. This offering will provide $850 million of new cash for the Treasury, as the regular 13-week and 26-week bill maturities were issued in the amount of $11,156 million. The $5,008 million of additional issue 50-day cash management bills issued December 1, 1982, and maturing January 20, 1983, will be redeemed at maturity.

The $11,156 million of regular maturities includes $1,318 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and $1,713 million currently held by Federal Reserve Banks for their own account. The two series offered are as follows:

91-day bills (to maturity date) for approximately $6,000 million, representing an additional amount of bills dated April 22, 1982, and to mature April 21, 1983 (CUSIP No. 912794 CB 8), currently outstanding in the amount of $10,894 million, the additional and original bills to be freely interchangeable.

182-day bills for approximately $6,000 million, to be dated January 20, 1983, and to mature July 21, 1983 (CUSIP No. 912794 DJ 0.)

Both series of bills will be issued for cash and in exchange for Treasury bills maturing January 20, 1983. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

R-1095

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, January 17, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on January 20, 1983, in cash or other immediately-available funds or in Treasury bills maturing January 20, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS
partment of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. January 12, 1983

TREASURY TO AUCTION $7,250 MILLION OF 2-YEAR NOTES

The Department of the Treasury will auction $7,250 million of 2-year notes to refund $4,647 million of 2-year notes maturing January 31, 1983, and to raise $2,603 million new cash. The $4,647 million of maturing 2-year notes are those held by the public, including $677 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities.

The $7,250 million is being offered to the public, and any amounts tendered by Federal Reserve Banks as agents for foreign and international monetary authorities (including the $677 million of maturing securities) will be added to that amount.

In addition to the public holdings, Government accounts and Federal Reserve Banks, for their own accounts, hold $544 million of the maturing securities that may be refunded by issuing additional amounts of the new notes at the average price of accepted competitive tenders.

Details about the new security are given in the attached highlights of the offering and in the official offering circular.

oOo

Attachment

R-1096

HIGHLIGHTS OF TREASURY
OFFERING TO THE PUBLIC
OF 2-YEAR NOTES
TO BE ISSUED JANUARY 31, 1983

January 12, 1983

Amount Offered:

To the public	$7,250 million

Description of Security:

Term and type of security	2-year notes
Series and CUSIP designation	Series Q-1985 (CUSIP No. 912827 PB 2)
Maturity date	January 31, 1985
Call Date	No provision
Interest rate	To be determined based on the average of accepted bids
Investment yield	To be determined at auction
Premium or discount	To be determined after auction
Interest payment dates	July 31 and January 31
Minimum denomination available	$5,000

Terms of Sale:

Method of sale	Yield Auction
Competitive tenders	Must be expressed as an annual yield, with two decimals, e.g., 7.10%
Noncompetitive tenders	Accepted in full at the average price up to $1,000,000
Accrued interest payable by investor	None
Payment by non-institutional investors	Full payment to be submitted with tender
Deposit guarantee by designated institutions	Acceptable

Key Dates:

Deadline for receipt of tenders	Wednesday, January 19, 1983, by 1:30 p.m., EST
Settlement date (final payment due from institutions)	
a) cash or Federal funds	Monday, January 31, 1983
b) readily collectible check	Thursday, January 27, 1983

TREASURY NEWS
partment of the Treasury • Washington, D.C. • Telephone 566-204

FOR IMMEDIATE RELEASE
January 13, 1983

CONTACT: Charles Powers
202/566-2041

CHARLES RINKEVICH SELECTED AS THE DIRECTOR,
FEDERAL LAW ENFORCEMENT TRAINING CENTER,
GLYNCO, GEORGIA

Secretary of the Treasury Donald T. Regan announced today that Charles F. Rinkevich of Marietta, Georgia, has been selected as the Director of the Federal Law Enforcement Training Center (FLETC), Glynco, Georgia.

FLETC, a bureau of the Department of the Treasury, is an interagency service organization for Federal law enforcement personnel from 49 participating organizations. Recently, FLETC also was designated by President Reagan to be the focal point for the creation of a National Center for State and Local Law Enforcement Training.

John M. Walker, Jr., Assistant Secretary (Enforcement and Operations), whose office has oversight responsibility for FLETC, commented that "Mr. Rinkevich is a superb choice to head this Nation's premier law enforcement training facility because of his extensive experience and knowledge of enforcement activities at all levels of government."

Mr. Rinkevich is a Regional Director for the U.S. Department of Justice's Audit Staff in Atlanta, Georgia. He is currently serving and will continue to serve as the Coordinator for the South Florida Task Force which was established by the President to counteract serious crime problems stemming from massive illegal immigration and drug smuggling into the United States through South Florida. Previously, he was assigned as Director of the Atlanta Federal Task Force which coordinated Federal assistance to the City of Atlanta during its crisis involving murdered and missing children. Mr. Rinkevich has also held important positions with the U.S. Law Enforcement Assistance Administration and the Pennsylvania Governor's Justice Commission. He served as a police officer in Michigan, a police training officer in Savannah, Georgia and law enforcement consultant with both the University of Georgia and the International Association of Chiefs of Police.

Mr. Rinkevich received an A.A. from Grand Rapids Junior College, Grand Rapids, Michigan, and a B.S. in Police Administration/Public Administration from Michigan State University, and he is nearing the completion of a masters degree in Public Administration from Georgia State University, Atlanta, Georgia. He is a recipient of the Department of Justice's Meritorious Award. His wife Sara and he have two children, Charles Jr., 11, and Monica, 9.

R-1097

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 12:00 NOON January 14, 1983

TREASURY'S 52-WEEK BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for approximately $7,500 million of 364-day Treasury bills to be dated January 27, 1983, and to mature January 26, 1984 (CUSIP No. 912794 EC 4). This issue will provide about $2,200 million new cash for the Treasury, as the maturing 52-week bill was originally issued in the amount of $5,294 million. The $4,006 million of additional issue 73-day cash management bills issued November 15, 1982, and maturing January 27, 1983, will be redeemed at maturity.

The bills will be issued for cash and in exchange for Treasury bills maturing January 27, 1983. In addition to the maturing 52-week and cash management bills, there are $11,162 million of maturing bills which were originally issued as 13-week and 26-week bills. The disposition of this latter amount will be announced next week. Federal Reserve Banks as agents for foreign and international monetary authorities currently hold $1,542 million, and Federal Reserve Banks for their own account hold $2,481 million of the maturing bills. These amounts represent the combined holdings of such accounts for the three regular issues of maturing bills. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average price of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them. For purposes of determining such additional amounts, foreign and international monetary authorities are considered to hold $325 million of the original 52-week issue.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. This series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Thursday, January 20, 1983. Form PD 4632-1 should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

R-1098

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders, the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on January 27, 1983, in cash or other immediately-available funds or in Treasury bills maturing January 27, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS
epartment of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE

January 17, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $ 6,000 million of 13-week bills and for $6,000 million of 26-week bills, both to be issued on January 20, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing April 21, 1983			:	26-week bills maturing July 21, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	98.091a/	7.552%	7.81%	:	96.132b/	7.651%	8.07%
Low	98.066	7.651%	7.91%	:	96.084	7.746%	8.17%
Average	98.074	7.619%	7.88%	:	96.093	7.728%2/	8.15%

a/ Excepting 4 tenders totaling $1,945,000.
b/ Excepting 2 tenders totaling $2,000,000.

Tenders at the low price for the 13-week bills were allotted 33%.
Tenders at the low price for the 26-week bills were allotted 66%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 43,005	$ 43,005	:	$ 94,495	$ 42,795
New York	8,982,095	4,440,295	:	10,866,315	4,942,850
Philadelphia	25,900	25,900	:	59,300	59,300
Cleveland	74,975	59,975	:	59,925	54,925
Richmond	37,130	37,130	:	25,470	25,470
Atlanta	49,455	47,220	:	35,220	35,220
Chicago	1,003,045	456,045	:	649,360	221,860
St. Louis	49,530	41,530	:	47,190	34,190
Minneapolis	15,105	14,435	:	14,590	9,590
Kansas City	42,910	42,210	:	38,660	38,660
Dallas	29,225	29,225	:	18,650	18,650
San Francisco	764,700	482,310	:	793,995	203,995
Treasury	281,205	281,205	:	312,840	312,840
TOTALS	$11,398,280	$6,000,485	:	$13,016,010	$6,000,345
Type					
Competitive	$ 9,558,300	$4,360,505	:	$10,539,940	$3,724,275
Noncompetitive	914,250	914,250	:	688,870	688,870
Subtotal, Public	$10,472,550	$5,274,755	:	$11,228,810	$4,413,145
Federal Reserve	913,030	713,030	:	800,000	600,000
Foreign Official Institutions	12,700	12,700	:	987,200	987,200
TOTALS	$11,398,280	$6,000,485	:	$13,016,010	$6,000,345

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 7.874%.

R-1099

FOR IMMEDIATE RELEASE JANUARY 17, 1983

The Treasury announced today that the 2-1/2 year Treasury yield curve rate for the five business days ending January 17, 1983, averaged 9.30 % rounded to the nearest five basis points. Ceiling rates based on this rate will be in effect from Tuesday, January 18, 1983 through Monday, January 31, 1983.

Detailed rules as to the use of this rate in establishing the ceiling rates for small saver certificates were published in the Federal Register on July 17, 1981.

Small saver ceiling rates and related information is available from the DIDC on a recorded telephone message. The phone number is (202)566-3734.

Approved ______________________
Francis X. Cavanaugh, Director
Office of Government Finance
& Market Analysis

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. January 18, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $12,000 million, to be issued January 27, 1983. This offering will provide $850 million of new cash for the Treasury, as the regular 13-week and 26-week bill maturities were issued in the amount of $11,162 million. The two series offered are as follows:

91-day bills (to maturity date) for approximately $6,000 million, representing an additional amount of bills dated October 28, 1982, and to mature April 28, 1983 (CUSIP No. 912794 CS 1), currently outstanding in the amount of $8,630 million, the additional and original bills to be freely interchangeable.

182-day bills for approximately $6,000 million, to be dated January 27, 1983, and to mature July 28, 1983 (CUSIP No. 912794 DK 7).

Both series of bills will be issued for cash and in exchange for Treasury bills maturing January 27, 1983. In addition to the maturing 13-week and 26-week bills, there are $5,294 million of maturing 52-week bills and $4,006 million of maturing cash management bills. The disposition of these latter amounts was announced last week. Federal Reserve Banks, as agents for foreign and international monetary authorities, currently hold $1,574 million, and Federal Reserve Banks for their own account hold $2,481 million of the maturing bills. These amounts represent the combined holdings of such accounts for the three regular issues of maturing bills.

Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them. For purposes of determining such additional amounts, foreign and international monetary authorities are considered to hold $1,249 million of the original 13-week and 26-week issues.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

R-2000

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, January 24, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on January 27, 1983, in cash or other immediately-available funds or in Treasury bills maturing January 27, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE January 19, 1983

RESULTS OF AUCTION OF 2-YEAR NOTES

The Department of the Treasury has accepted $7,251 million of $14,341 million of tenders received from the public for the 2-year notes, Series Q-1985, auctioned today. The notes will be issued January 31, 1983, and mature January 31, 1985.

The interest rate on the notes will be 9-1/4%. The range of accepted competitive bids, and the corresponding prices at the 9-1/4% interest rate are as follows:

	Bids	Prices
Lowest yield	9.18% 1/	100.125
Highest yield	9.28%	99.946
Average yield	9.25%	100.000

Tenders at the high yield were allotted 42%.

TENDERS RECEIVED AND ACCEPTED (In Thousands)

Location	Received	Accepted
Boston	$ 79,780	$ 58,740
New York	11,623,495	5,727,575
Philadelphia	48,835	48,255
Cleveland	179,315	155,355
Richmond	175,395	143,330
Atlanta	119,860	111,830
Chicago	1,103,580	405,620
St. Louis	167,975	109,805
Minneapolis	77,430	77,430
Kansas City	136,270	132,290
Dallas	30,960	26,720
San Francisco	593,325	248,725
Treasury	4,920	4,920
Totals	$14,341,140	$7,250,595

The $7,251 million of accepted tenders includes $1,338 million of noncompetitive tenders and $5,913 million of competitive tenders from the public.

In addition to the $7,251 million of tenders accepted in the auction process, $420 million of tenders was awarded at the average price to Federal Reserve Banks as agents for foreign and international monetary authorities. An additional $544 million of tenders was also accepted at the average price from Government accounts and Federal Reserve Banks for their own account in exchange for maturing securities.

1/ Excepting 3 tenders totaling $4,010,000.

R-2001

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE

January 20, 1983

RESULTS OF TREASURY'S 52-WEEK BILL AUCTION

Tenders for $ 7,501 million of 52-week bills to be issued January 27, 1983, and to mature January 26, 1984, were accepted today. The details are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:

	Price	Discount Rate	Investment Rate (Equivalent Coupon-issue Yield)
High -	91.931	7.980%	8.62%
Low -	91.893	8.018%	8.66%
Average -	91.904	8.007%	8.65%

Tenders at the low price were allotted 40%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted
Boston	$ 51,140	$ 24,640
New York	14,315,750	6,529,150
Philadelphia	27,730	20,730
Cleveland	43,050	19,550
Richmond	78,010	68,005
Atlanta	66,190	34,190
Chicago	1,186,880	439,380
St. Louis	67,535	38,035
Minneapolis	38,195	21,570
Kansas City	60,510	52,010
Dallas	18,250	13,250
San Francisco	1,000,475	170,985
Treasury	69,970	69,970
TOTALS	$17,023,685	$7,501,465
Type		
Competitive	$15,330,945	$5,808,725
Noncompetitive	512,740	512,740
Subtotal, Public	$15,843,685	$6,321,465
Federal Reserve	900,000	900,000
Foreign Official Institutions	280,000	280,000
TOTALS	$17,023,685	$7,501,465

R-2002

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE

January 24, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $ 6,004 million of 13-week bills and for $6,014 million of 26-week bills, both to be issued on January 27, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing April 28, 1983			:	26-week bills maturing July 28, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	97.972a/	8.023%	8.30%	:	95.890	8.130%	8.60%
Low	97.960	8.070%	8.35%	:	95.881	8.147%	8.62%
Average	97.964	8.055%	8.34%	:	95.883	8.144%2/	8.61%

a/ Excepting 1 tender of $995,000.

Tenders at the low price for the 13-week bills were allotted 96%.
Tenders at the low price for the 26-week bills were allotted 91%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 47,945	$ 47,945	:	$ 34,885	$ 24,885
New York	11,331,175	4,589,535	:	13,522,600	5,403,255
Philadelphia	28,190	28,190	:	26,140	17,640
Cleveland	88,660	52,160	:	82,640	19,840
Richmond	53,470	36,670	:	100,625	30,625
Atlanta	51,985	47,015	:	122,630	29,685
Chicago	991,000	149,000	:	989,155	54,635
St. Louis	41,835	39,585	:	42,685	34,435
Minneapolis	19,635	13,635	:	18,075	11,020
Kansas City	46,115	45,800	:	40,575	40,575
Dallas	29,670	24,670	:	16,310	11,310
San Francisco	1,270,385	650,705	:	1,085,220	43,325
Treasury	278,875	278,875	:	292,410	292,410
TOTALS	$14,278,940	$6,003,785	:	$16,373,950	$6,013,640
Type					
Competitive	$12,431,825	$4,306,670	:	$14,228,275	$4,017,965
Noncompetitive	975,080	975,080	:	722,775	722,775
Subtotal, Public	$13,406,905	$5,281,750	:	$14,951,050	$4,740,740
Federal Reserve	831,035	681,035	:	750,000	600,000
Foreign Official Institutions	41,000	41,000	:	672,900	672,900
TOTALS	$14,278,940	$6,003,785	:	$16,373,950	$6,013,640

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 7.898%.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. January 25, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $12,000 million, to be issued February 3, 1983. This offering will provide $825 million of new cash for the Treasury, as the maturing bills are outstanding in the amount of $11,187 million, including $1,131 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and $1,529 million currently held by Federal Reserve Banks for their own account. The two series offered are as follows:

91-day bills (to maturity date) for approximately $6,000 million, representing an additional amount of bills dated November 4, 1982, and to mature May 5, 1983 (CUSIP No. 912794 CT 9), currently outstanding in the amount of $5,628 million, the additional and original bills to be freely interchangeable.

182-day bills for approximately $6,000 million, to be dated February 3, 1983, and to mature August 4, 1983 (CUSIP No. 912794 DL 5).

Both series of bills will be issued for cash and in exchange for Treasury bills maturing February 3, 1983. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

R-2004

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, January 31, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on February 3, 1983, in cash or other immediately-available funds or in Treasury bills maturing February 3, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
January 25, 1983

Contact: Robert E. Nipp
(202) 566-2133

TREASURY ANNOUNCES PRICE INCREASES FOR OLYMPIC COINS

The Treasury Department today announced that the cost of Olympic coins will be increased effective tomorrow, January 26. The increase reflects the upward movement in the price of precious metals, and the end of the pre-issue discount rate mandated by the Olympic Commemorative Coin Act. There will be an additional fee to help defray postage and handling costs. Orders mailed on or after January 26 will be accepted at the new rates only.

Public Law 97-220 signed by President Reagan on July 22, 1982, authorizes the Mint to strike three coins with designs emblematic of the summer Olympic games which are to be held in Los Angeles, California July 28 to August 12, 1984:

* A silver dollar coin bearing the 1983 date and composed of 90 percent silver. Production of the proof coin will begin early next month at the San Francisco Assay Office.

* A second 90 percent silver dollar coin of different design and bearing the 1984 date. It will be available early next year.

* A $10 gold coin bearing the 1984 date and composed of 90 percent fine gold (21.6 karat). This represents the first gold coin to be produced by the United States Mint in over 50 years and will be available in early 1984.

The silver coins will contain .77 troy ounces of silver and have a diameter of 1.50 inches; the gold coins will contain .484 troy ounces of fine gold and have a diameter of 1.06 inches.

Public Law 97-220 provides that a surcharge of no less than $10 for each silver coin and $50 for each gold coin be used to promote the Olympic movement. These surcharges are incorporated into the costs of the coin sets. Specifically, the law stipulates that 50 percent of the surcharges be promptly paid to the United States Olympic Committee to be used to train United States Olympic athletes, to support local or community amateur athletic programs and to erect facilities for the training of such athletes. The remaining 50 percent of the surcharges shall be paid to the Los Angeles Olympic Organizing Committee to be used to stage and promote the 1984 games in Los Angeles.

(more)

The new prices on the three sets are effective through Tuesday, April 5, 1983. Prices after April 5 have not been established. In the event that further significant increases in bullion prices should occur, the Mint reserves the right to discontinue the acceptance of orders before April 5. Once an order is accepted by the Mint, however, it will not be cancelled due to changes in bullion prices. Interested buyers are invited to send a letter order and payment to:

The United States Mint
P. O. Box 6766
San Francisco, CA 94101

Those interested in bulk rate discounts should write Olympic Coin Program, 475 Park Avenue, South, New York, New York 10016.

The three options, their prices, and postage and handling charges effective January 26 are:

Single Coin Set

1983 Silver One Dollar Proof Coin	$29.00 plus postage & handling

Two Coin Set

1983 Silver One Dollar Proof Coin 1984 Silver One Dollar Proof Coin	$58.00 plus postage & handling

Three Coin Set

1983 Silver One Dollar Proof Coin 1984 Silver One Dollar Proof Coin 1984 Gold Ten Dollar Proof Coin	$410.00 plus postage & handling

A charge of $2.00 for the first set plus $1 for each additional set is being made to help defray postage and handling costs. Add this amount to the total cost of the coins.

The Treasury Department also reported that more than 800,000 Olympic coins have been sold through Friday, January 21 with gross sales in excess of $60 million. Of this amount, $14 million in surcharges have been collected for the two Olympic committees.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE UPON DELIVERY
EXPECTED AT 10 A.M.
Wednesday, January 26, 1983

TESTIMONY OF THE HONORABLE DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
JOINT ECONOMIC COMMITTEE

Mr. Chairman and Members of the Committee:

It is a pleasure to meet with you today to discuss the current state of the economy and the outlook for the future. Two years ago the incoming Reagan Administration inherited a very difficult economic situation. Real growth had declined steadily in the late 1970's and was negative by 1980. Inflation had soared to double digit levels. The ensuing two years have seen serious economic recession as a result of the inflation/tax spiral. On the bright side, inflation is down from 12.4 percent for 1980 to 3.9 for 1982.

However, the worst is over in the sense that signs such as housing, inventories, and real income show the economy is poised for recovery. Interest rates are down from peak levels of 21-1/2 percent on the prime to 11 percent currently and the stock market last year made new peaks. Alongside these favorable developments, there is the distressing fact of high levels of unemployment.

The task now is to encourage the renewal of economic growth to reduce unemployment and provide productive job opportunities in the private sector. But in so doing we must not repeat the errors of the past and return to an inflationary economy. That's been our past experience and it only leads to an even more severe adjustment at some time in the future. The correct course of action is to persevere with our policies that are designed to promote long-run economic growth while keeping inflation securely under control.

The current domestic situation is complicated by the existence of large federal budget deficits and the threat of even larger ones in the future. These budget deficits will have to be reduced since their persistence would inevitably lead to very adverse consequences for the U.S. economy and its financial markets.

Many of the economic difficulties we face at home are also faced by countries abroad. The entire international economy is experiencing a severe slowdown, complicated by the special debt-servicing problems of a number of countries. My prepared statement today deals primarily with the U.S. domestic economy, but it is obvious that the domestic and international situations are closely linked. The clear need in both cases is to encourage expansion rather than undergo further contraction.

The Background of Current Difficulties

There would be no point to a lengthy review of past developments. It is important to recognize, however, that current difficulties are the culmination of a long period of deteriorating economic performance in this country. The U.S. economy was in deep trouble long before the current recession began. It follows that our policies must aim at lasting long-run solutions. There are no quick cures.

The origin of most of our current difficulties was the failure to control inflation after the mid-1960's. Once underway, the inflationary process was fueled by excessive rates of monetary expansion and developed a momentum of its own. There have been intense periods of inflation before in this country, but only temporarily at, or near, wartime peaks. The Great Inflation of the 1960's and 1970's is without parallel in previous U.S. experience. As shown in Chart I, each cyclical peak and trough in the rate of inflation following the mid-1960's was at successively higher levels. The basic rate of inflation was finally ratchetted to double digit levels. Only now and at great cost has the upward trend of inflation been interrupted.

Rising rates of inflation after the mid-1960's did not lead to more rapid economic growth for any sustained period of time. Quite the contrary. Inflation and its inevitable consequence of higher interest rates finally choked off real growth altogether. As shown in Chart II, real growth averaged about 4 percent annually in the decades of the 1950's and 1960's, and slowed to a little over 3 percent in the 1970's. Indeed, by the late 1970's, real growth was nonexistent. And, since 1979 there have been two recessions and real growth has turned negative. Over most of this period of time while growth was declining, the rate of inflation moved upward more or less steadily.

Rising rates of inflation after the mid-1960's led to a roughly parallel rise in key interest rates. As shown in Chart III, the 3-month Treasury bill rate followed the rate of inflation very closely over most of the period. Thus, inflation appears to have been a major factor in the increase in the bill rate since the early 1960's.

Proposals to force down interest rates through monetary expansion fail to recognize that over long periods of time the absolute level of nominal interest rates is determined by an underlying real rate of interest plus a premium equal to the expected rate of inflation. Sustained periods of monetary expansion drive up the rate of inflation and pull up interest rates. The chart also shows very clearly the extent to which interest rates have risen above the inflation rate in the last few years of unusually violent swings in money growth. The resulting increase in real interest rates is due to what might be termed a wider risk or volatility premium -- in addition to the inevitable inflation premium.

The combination of inflation and rising interest rates was extremely harmful for the economy. The continuation of inflation over long periods of time encouraged the assumption of heavy debt burdens by individual and corporate borrowers in the belief that a new era of permanent inflation had commenced. Those debt burdens have become extremely heavy as the period of inflation has drawn to an end. Inflation also exerted a depressing effect on corporate profitability both because of inadequate financial provision for the replacement of real capital and because of the unremitting pressure of wage demands to keep pace with increases in the cost of living and rising tax rates.

The combined effect of rising interest rates and downward pressure on profit margins is shown in Chart IV. The share of profits in national income has fallen more or less steadily since the mid-1960's while the interest share has risen. Both of these trends have accelerated in recent years. Some of the recent rise in net interest may simply reflect the deregulation of financial markets -- a healthy development. But, the long period of inflation offered unhealthy incentives for borrowing and reduced the share of profits in national income.

By late 1980, the U.S. economic and financial situation had reached a very difficult stage. Critics would do well to recall the state of affairs which this Administration inherited, as I stated earlier.

Approach of the Reagan Administration

The Administration's primary economic goal upon coming to office was to reverse the situation. In our view that required a fundamental restructuring of the economy, including:

- bringing inflation under control;
- shifting the composition of activity away from government spending and toward the private sector into more productive endeavors;

- providing an environment which would reward innovation, work effort, saving and investment, and in which free-market forces could operate effectively.

Within a month of coming into office, President Reagan put before Congress a four-point program designed to reverse the steadily deteriorating performance of the past decade and a half. That program consisted of:

- spending restraint;
- tax reductions;
- far-reaching regulatory improvements;
- gradual, steady reduction in the rate of monetary growth to a pace consistent with noninflationary expansion of the economy.

While we did not get our full package through Congress in the exact form we had asked for, our success in achieving quick approval of the major elements of the program was unprecedented. This support doubtless reflected widespread recognition that restoring vitality to the economy would require broadscale revamping of fiscal and monetary policies.

Over the past two years we have seen evidence that the program is working. We have made very significant gains on the inflation front and we are now witnessing a reduction in interest rates, both of which are prerequisites for a resumption of solid economic growth.

- In the twelve months ending in December consumer prices rose only 3.9 percent -- far below the back-to-back double-digit increases of 13.3 percent and 12.4 percent in 1979 and 1980 and the smallest rise since price controls artificially depressed the statistic in 1972. The broadest measure of inflation, the GNP deflator, has come down by more than half since 1980 to an increase of only 4.6 percent during 1982. These statistics mark an achievement of primary importance in restoring economic vitality. The inflationary spiral has been reversed, thereby conquering the major economic problem of the past decade and a half.

- The reduction in inflationary pressures has also been visible in wages. But because prices had risen less, there was good news on wages for the employed people of this country. The average hourly earnings index increased only 5.9 percent in the twelve months ending in December, the smallest rise since 1967. Nonetheless, after four years in which workers had seen the steady erosion of the purchasing power of their earnings, 1982 was the first time since 1977 in which a real wage gain was posted. (Chart V shows the recent record on earnings and price growth.)

- It took somewhat longer than hoped for interest rates to come down. Rates remained sticky through the spring of last year (Chart VI), stalling the widely anticipated recovery. However, as markets became aware that the progress on inflation was not transitory, interest rates began to drop. The prime fell from 21-1/2 percent in September 1981 to 11 percent currently -- a dramatic reduction. The three-month Treasury bill rate has also fallen by about 500 basis points from the end of June to about 8 percent currently and is down by more than half from its peak. Yields on Aaa corporate bonds are now about 11-3/4 percent, a drop of a little over 300 basis points since last June.

- The decline in interest rates was certainly at least in part responsible for triggering the phenomenal stock market rally that took place this fall. Stock prices are now running more than 35 percent above their August lows, contributing signficantly to household wealth.

We have strong evidence that the fundamental elements of recovery are now largely in place. Inflation has been brought under control. Interest rates are coming down. Real wage growth is being restored. In addition, there have been other improvements -- notably in productivity growth and saving behavior -- which mark a shift away from the problems that contributed to sluggish economic performance in recent years.

- During the latest recession the falloff in productivity has been less than normal, apparently reflecting vigorous efforts by business to reduce costs. Productivity in the total business sector turned positive in the second quarter of last year and scored a strong 4.2 percent annual rate of advance in the third quarter. Gains in productivity are usually greatest in the early stages of recovery so we can look forward to further progress as real growth resumes. Since high productivity reduces costs per unit of output, this will help ensure that inflationary pressures are not reignited when the recovery gets underway.

- The personal saving rate has also registered improvement since the first portions of the Administration's tax rate reductions and savings incentives were put into effect in October 1981. In the five quarters since then, the personal saving rate has averaged 6.7 percent, up from the 5.9 percent rate that prevailed from 1977 through 1980.

Within this framework of very significant achievements, there remains the fact that the economy has been in recession and unemployment is high.

. The unemployment rate of 10.8 percent in December is, of course, a matter of great concern. It is important to remember, however, that in December the share of the working-age population with jobs was 56.5 percent -- 1-1/2 percentage point above the 1975 low and close to the peaks reached in the 1960's. (See Chart VII.)

The Current State of the Economy

The economy now stands poised for recovery. In fact, the recovery may well already be underway at this moment. It is always some time after the fact before the actual month of turnaround can be pinpointed.

The recovery has been much longer in coming than we had expected, or, for that matter, than expected by nearly all forecasters. Last year at this time we were projecting that improvement in the economy would begin to emerge in the spring and that growth during the four quarters of 1982 would be 3.0 percent. This was almost exactly the consensus of private forecasters, as contained in Blue Chip Economic Indicators of January 1982, which projected real growth of 3.1 percent during the year. Last summer the economy appeared to be in the process of turning around, and we, along with the private forecasting community, projected recovery in the second half of the year. The delayed coming of the recovery has been a major disappointment.

The recovery was delayed primarily because of the persistence of high interest rates and because of developments in the international sphere. Interest rates remained intractably high into the summer. Rates in general tend to be slow to change on the way down. Additionally this year, inflationary expectations failed to incorporate fully the rapidly proceeding process of disinflation. On the international front, the economies of our leading trading partners continued to weaken. Industrial production of OECD European countries dropped at an 8 percent annual rate between the first and third quarters of last year, and production in Japan was unchanged. Weakness among all the industrialized nations was self-reinforcing. Furthermore, the financial difficulties of some of the newly industrializing nations had adverse impacts on economic activity here. To cite but one example, our exports to Mexico were down in October and November by about 60 percent from a year earlier, or nearly $11 billion measured at an annual rate. Overall, the slide in total real net exports accounted for nearly one-half of the total decline in real GNP between the third quarter of 1981 and the final quarter of last year. These forces, combined with a general hesitancy on the part of the consumer, led to another round of inventory cutting in the second half of 1982 and delayed the expected turnaround of the economy.

Signals of an Economic Upturn

There are clear signals that the economy is turning around now and that the recession will soon be behind us. To summarize these signals:

- The index of leading indicators has risen for seven out of the last eight months.

- Housing is in the midst of a rapid recovery. New home starts jumped by 45 percent in the fourth quarter from a year earlier; and permits increased by 60 percent over the same span. As shown in Chart VIII, new home sales have risen 55 percent since the spring quarter of last year, and inventories of unsold homes have hit the lowest levels recorded in more than a decade.

- Business trimmed inventories sharply in the final quarter of last year -- a 6 percent annual rate for the nonfarm sector. Historically, a cleanout of inventories typically has been followed by a shift back to higher rates of production.

- Retail sales have begun to firm. Sales of the major nonautomotive discretionary components of consumer purchasing -- namely household durables and clothing -- rose at an impressive 11-1/2 percent annual rate in real terms in the final three months of last year. Automobile sales appear to be in the early stages of recovery, following a four-year period of decline. Auto production is slated to rise by 20 percent (not annualized) in the first quarter of this year from the prior quarter, and that increase could be even larger should sales continue to outpace currently announced production schedules.

- Total industrial production stabilized in December and appears poised to turn upward.

- Weekly initial claims for state unemployment insurance have been trending downward since mid-October. And even though employment continued to decline in December, decreases in recent months have slowed notably.

- Finally, declines in interest rates and the resurgence of stock prices since last summer are indicative of a vastly improved financial climate.

The Typical Recovery

We would all hope for a vigorous recovery, not unlike those which occurred in the past. The typical postwar recovery path is shown in Chart IX. Excluded from it are the two atypical recoveries -- the first of which included the Korean War buildup and the second which got underway late in 1980 but was short-lived. The five recoveries contained in the average line in the chart were remarkably similar. Gains over the first eight quarters from the real GNP trough were within an extremely narrow range of 10.2 percent to 12.0 percent -- in the 5 to 6 percent annual rate range.

The contributions of GNP components to real growth during the typical recovery are shown in Chart X. Notably, that chart clearly indicates that stimulus from higher Federal spending is not a prerequisite for strong recovery. In fact, real Federal purchases declined on average during previous recoveries, and especially so during their early stages. Furthermore, improvement in our real balance of net exports also is not necessary for strong recovery, as it too has typically weakened during the early stages of recovery. Real capital spending typically contributed but little to the early stages of recovery, though picking up steam in the second year.

As the chart indicates, much of the initial thrust for expansion comes from:

- A resurgence in homebuilding activity, such as currently is underway.

- A swing in inventory investment from decumulation in the later stages of recession to accumulation. Decumulation proceeded rapidly in the fourth quarter of last year, apparently setting the stage for a swing upward in inventory investment over coming quarters.

- A major contribution from consumer spending, with purchases of consumer durables registering particularly large increases. Consumers recently have vastly improved their financial positions, and with the age of existing stocks of consumer durables, most importantly of autos, having increased substantially over the past several years, coming quarters should witness a rebound in consumer spending.

The Outlook for the Economy

A vigorous recovery of the type outlined would be most welcome. It would certainly help ease the Nation's budgetary problems. If, for example, real GNP growth was only 0.5 percent higher than our current forecast in 1983 and 1984, the deficit would decline to $90 billion in 1988 instead of the $117 billion estimated in the budget. If real GNP growth reached the high rates obtained during the early 1960's (1.3% higher growth in each of the next six years) we could balance the budget by 1988. However, we recognize that the serious problems still confronting us may well hold growth during the next year or two below the typical recovery pattern.

- Our overall trade balance is likely to register further marked deterioration in the coming year, reflecting the recent high value of the dollar and the serious problems of our trading partners.

- Real interest rates may persist at high levels though far below those prevailing a year ago.

- The economy is in the process of undergoing marked structural change. Some of our industries may not quickly regain the vitality they experienced in the 1950's and 1960's. The shift of resources to emerging industries will take time.

- The transition to a noninflationary environment is not an easy one. In particular, as inflation is winding down, businesses face uncertain returns on investment programs, as they will not know what prices they may be able to charge in the future. Only one thing is certain -- they will not be able to count on ever accelerating inflation to bail out faulty investment decisions.

- Most fundamentally, we are not yet fully out of the inflationary woods, and we cannot afford to direct monetary and fiscal policy toward excessively rapid economic expansion. Rather, we must set our sights on achieving a steady, stable, long-lived expansion, one in which inflation can be further reduced and the conditions for rapid growth of productivity and living standards can be fostered.

For these reasons, the Administration will be forecasting fairly modest real growth at a 3 percent rate during the four quarters of 1983, rather than the typical recovery growth rate of about twice that much. Certainly we would welcome a strong recovery. Growth is expected to pick up modestly to the 4 percent range in 1984 and the years beyond.

If we are successful in making this difficult transition and move onto a sustainable, noninflationary growth path, then we can look forward to years of improved economic performance such as we enjoyed during the 1950's and in the early 1960's. Such a growth path can only be achieved by consistent application of the proper mix of policies. It will certainly require that we take immediate and strenuous efforts to reduce the budget deficits that loom ahead.

Policies for the Recovery

In setting policy for the remainder of the 1980's, we must recognize what we must not do. We no longer have the freedom of action to revert back to the overly stimulative monetary and fiscal policies pursued at times in the past, for these would surely lead to a resurgence of inflationary pressures and a new round of rising interest rates. Further, we must not reverse the fundamental tax restructuring put in place in 1981, for this was designed to provide the noninflationary incentives without which the private sector would continue to wither.

Sound policy for the remainder of the 1980's must build on the framework enunciated by the President two years ago. That program was designed to foster an economic climate in which the private sector could flourish. The problems facing us are even more severe than we envisaged two years ago, but we still believe the general course laid out then was the proper one.

Monetary Policy

Achievement of a gradual slowing of growth in the money supply to a steady and noninflationary pace has been, and continues to be, one of the major goals of the Administration's economic program. The Federal Reserve's efforts to achieve that goal have been complicated by a number of factors such as by far-reaching institutional changes in the banking and thrift industries. Nevertheless, the Fed has generally succeeded in its efforts albeit in a somewhat erratic fashion: in the four years ending in 1980, growth in the money supply (M1) from fourth quarter to fourth quarter averaged nearly 8 percent annually. In 1981, M1 growth slowed sharply to a 5 percent rate, and from the fourth quarter of 1981 to the third quarter of 1982 M1 grew at only a 5.3 percent annual rate.

The Federal Reserve's efforts to slow money growth have, however, been accompanied by some volatile short-run swings. Growth in the narrowest monetary aggregate, M1, was actually negative on a 13-week basis by mid-summer of last year, and then soared to the double-digit range by the end of the year. This recent acceleration has caused some observers to conclude that the fight against inflation and inflationary money growth has been abandoned. That is not true. Both the Administration and the Federal Reserve remain committed to the long-run goal of providing money growth at a noninflationary pace consistent with a steady and sustainable expansion of economic activity.

Monetary policy faced a difficult and uncertain situation during much of last year. Rapid institutional change in the form of new money market instruments blurred the boundaries between the various aggregates and made the achievement of any target rates of growth unusually difficult. There is also some indication that the recession may have led to an increased demand for liquidity and precautionary balances. In 1982, growth in monetary velocity -- the rate at which money is used -- turned negative for the first time in nearly three decades as shown in Chart XI. Under the unusual economic and institutional circumstances of 1982, some temporary offset in the form of above-target rates of monetary growth was probably desirable.

As we look to the year ahead, it is clear that monetary policy goals will be important. Interest rates are still higher than they should be, and money growth must be returned eventually to the steady noninflationary pace envisioned by our overall economic program. One of the reasons interest rates remain high is that markets continue to be uncertain about the direction of Federal Reserve policy in the short run. The erratic movement of the money supply has been a factor underlying that uncertainty, and we hope that an even greater effort to avoid the wide swings in money growth seen in 1981 and 1982 will be undertaken by the Federal Reserve. Some of those fluctuations, of course, were the result of the institutional changes which have occurred and which have blurred the meaning of the traditional money supply measures. Nevertheless, as flows to and from the new money market deposit accounts and Super NOW accounts settle down and economic recovery moves ahead, the stage will be set for the Fed to follow a policy aimed once again at steady, predictable and noninflationary money growth.

Fiscal Policy

The objectives of our fiscal policy upon coming to office two years ago were two-fold. First, we believed and still believe it was imperative to correct the disincentives to economic performance that had been built into the tax structure over the years. These disincentives arose in large measure, not by design, but through the interaction of a high rate of inflation with a progressive tax system and historical cost accounting of depreciable assets. Second, it was equally imperative to reverse the seemingly inexorable growth of Federal spending, thereby freeing resources for use in the private sector.

The tax reforms that were put in place were designed primarily to restore an adequate rate of return of investment in plant and equipment and to put a halt to the steady upcreep of marginal tax rates on labor and savings income. The investment incentives were necessary to bring long-depressed U.S. investment rates and productivity growth rates up to acceptable standards. These measures will greatly improve our competitive standing in the world as economic recovery proceeds. For individuals, the tax cuts were needed to protect incentives and purchasing power. For the average taxpayer, they will only result in an actual dollar tax cut in 1983, after allowance for the effects of bracket creep and higher social security taxes. And that 1983 cut will be needed to offset scheduled increases in social security taxes in the future.

Even with the tax reforms fully in place in 1984, the marginal tax rate on American labor will be in the 40 percent range, including social security as well as Federal and State and local income taxes. For example, Mr. Chairman, a $25,000 a year worker with three dependents in the State of Iowa who does not itemize will be in the 22 percent Federal income tax bracket and the 8 percent state income tax bracket, and will face a combined marginal income tax rate of 30 percent. In addition, the worker and his employer will face a combined payroll tax of more than 13 percent, for a total tax on additional wages of over 43 percent. In recent years, it has cost a firm close to $1.70 to reward a worker with an additional $1.00 of compensation, a difference which can only be paid out of productivity gains.

It is of utmost importance that we do not revert to old policies by repealing the indexation to become effective in 1985 and relying on inflation to provide hidden, unlegislated increases in tax rates. What is needed now is not a reversal of previous reforms in the tax structure, but additional reforms to provide for even further reductions in disincentives. We will be taking a careful look at the structure of the entire tax system over the coming year.

We were relatively successful in working with the Congress to achieve our goals of tax reform, but we were less successful in the area of outlay control. While some of our proposals for outlay reduction were enacted in the Omnibus Budget Reconciliation Act of 1981 and in the First Concurrent Budget

Resolution of 1982, a major portion of the savings we hoped to achieve did not receive favorable action. This, along with much weaker economic activity than expected, has left us facing the prospect of large deficits even as the economy recovers. Deficits can feed on deficits, as each year's deficit raises the debt servicing costs for the forthcoming year.

This Administration has determined that deficits of the magnitudes bandied about in the press lately will not come to pass. Deficits of such size would drain the available savings pool, force up interest rates, and dampen spending on new business plant and equipment. This Administration came to office with a program of boosting the rate of capital investment in order to place the economy on a faster growth track, and we will not allow ourselves to be diverted from that goal. We will take whatever measures are necessary to narrow the deficit to acceptable levels. Preferably, the deficit can be narrowed from the outlay side. Total federal spending represents the amount of resources absorbed by the government at the expense of the private sector. This spending is financed by both taxes and borrowing, which in either case amounts to a drain on private savings. Only through spending reduction will the credit market find itself in a more favorable position. However, if we are not successful in reducing outlays sufficiently, and deficits still loom in the outyears even as the economy recovers, we are prepared to request additional revenue raising measures to be effective in those years. If the Congress chooses not to reduce spending, as we wish, then it is preferable to have the full cost of federal spending programs explicitly identified for the taxpayers who bear the burden of financing government. In the event taxes are needed, this Administration will do its best to structure the tax code in a way that minimizes disincentives for productive effort.

Policies for a Changing Economic Structure

Not only must we maintain steady monetary and fiscal policies directed at reinvigorating the private sector of the economy, but we must carry through with policies of reducing the regulatory burden on private industry. Noteworthy successes have been achieved in this area, particularly in the deregulation of the financial system. For the first time in the postwar period, small investors can count on being able to obtain market rates of return on their savings from banks and thrift institutions.

Further, we recognize that our economy and those of the other industrialized nations are undergoing a period of rapid restructuring. This is an era of rapid technological change, and comparative advantage in the production of many goods and services is shifting from the already developed to the newly developing nations. These forces must be encouraged and fostered. Those nations which expend all their energies shoring up declining industries and resisting change will find themselves with industrial bases that are obsolete and with declining relative standards of living. Their more foresighted and innovative neighbors will be moving forward and capturing newly opening markets.

Government can ease this painful process, but the private sector must take primary responsibility for making this transition. In order to help smooth the process, the President has announced a program that relies heavily on the market mechanisms to deal with structural unemployment that stems from problems in both labor and product markets. Unlike cyclical unemployment, which will respond to the stimulus of economic recovery, structural unemployment requires more specific measures that address the unique problems of young people and the long-term unemployed. Thus, the President's program will emphasize training, retraining and relocation, and job-search assistance for workers facing the lack or loss of jobs even after an economic recovery. Other proposals will be designed to reduce the barriers to youth employment. Business management will face particularly difficult times, for they must develop their investment and new product strategies during times of both rapid transition to a noninflationary climate and rapid structural change. Individuals must exercise initiative in making the investment in human capital which will allow them to work effectively in this changing environment.

Finally, in setting the proper course of policy for the 1980's, we must work closely with the other industrialized nations of the world, so that we all can move forward together onto sustainable, noninflationary expansion paths. We must also work diligently and cooperatively to assist financially troubled newly industrializing nations to overcome their problems. The International Monetary Fund (IMF) plays an integral role in current efforts to promote the sound world economy and stable international financial system required for economic recovery in the United States and abroad. International negotiations are nearing completion on measures to assure that the IMF has adequate resources to help countries experiencing difficulties implement sound policies of economic adjustment. The participation of the United States in an increase in IMF resources is an essential complement to domestic measures to achieve sustainable economic growth and represents a valuable investment in defense of the economic interests of the American farmer, laborer, businessman, and consumer. Legislation providing for the U.S. share of the increase in IMF resources will be submitted in the near future and I urge prompt approval by the Congress.

Most important, all nations must eschew courses of protectionism in futile efforts to shift the burden of economic difficulties to others. Only through cooperation and common policies directed by common goals can we move forward together.

Chart I

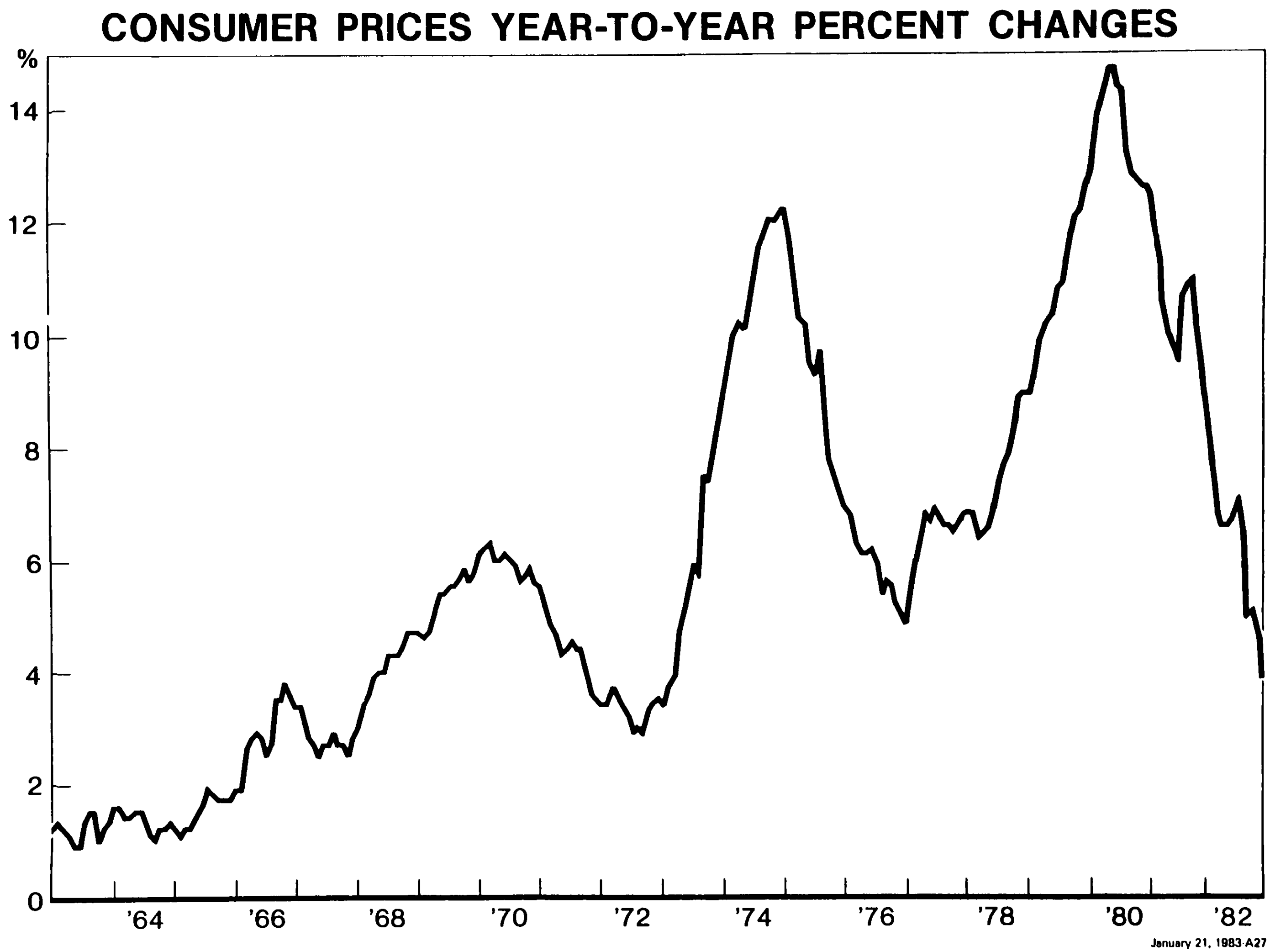

CONSUMER PRICES YEAR-TO-YEAR PERCENT CHANGES
%
14
12
10
8
6
4
2
0
'64
'66
'68
'70
'72
'74
'76
'78
'80
'82
January 21, 1983-A27

Chart II

ANNUAL RATES OF GROWTH OF REAL GNP AND INFLATION

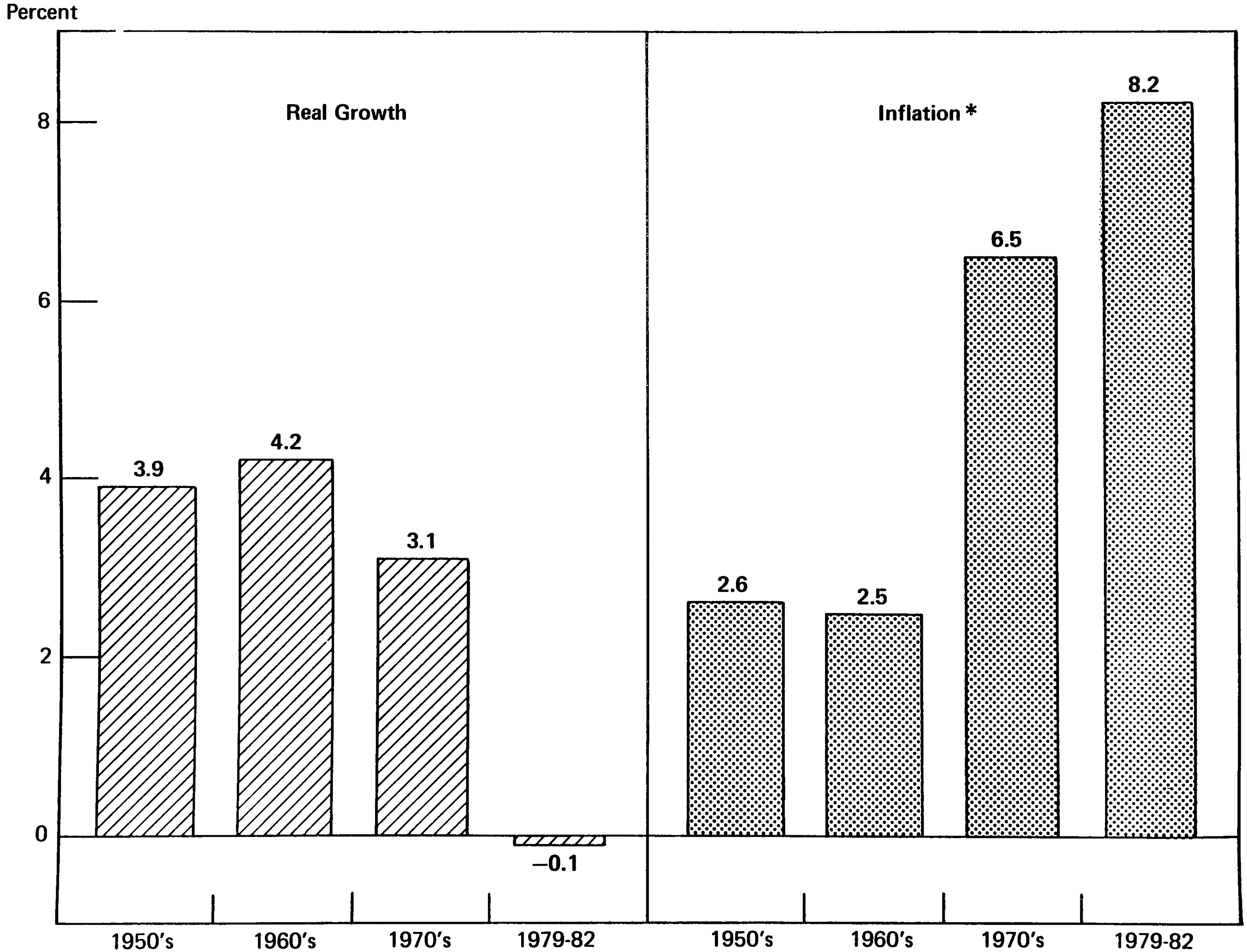
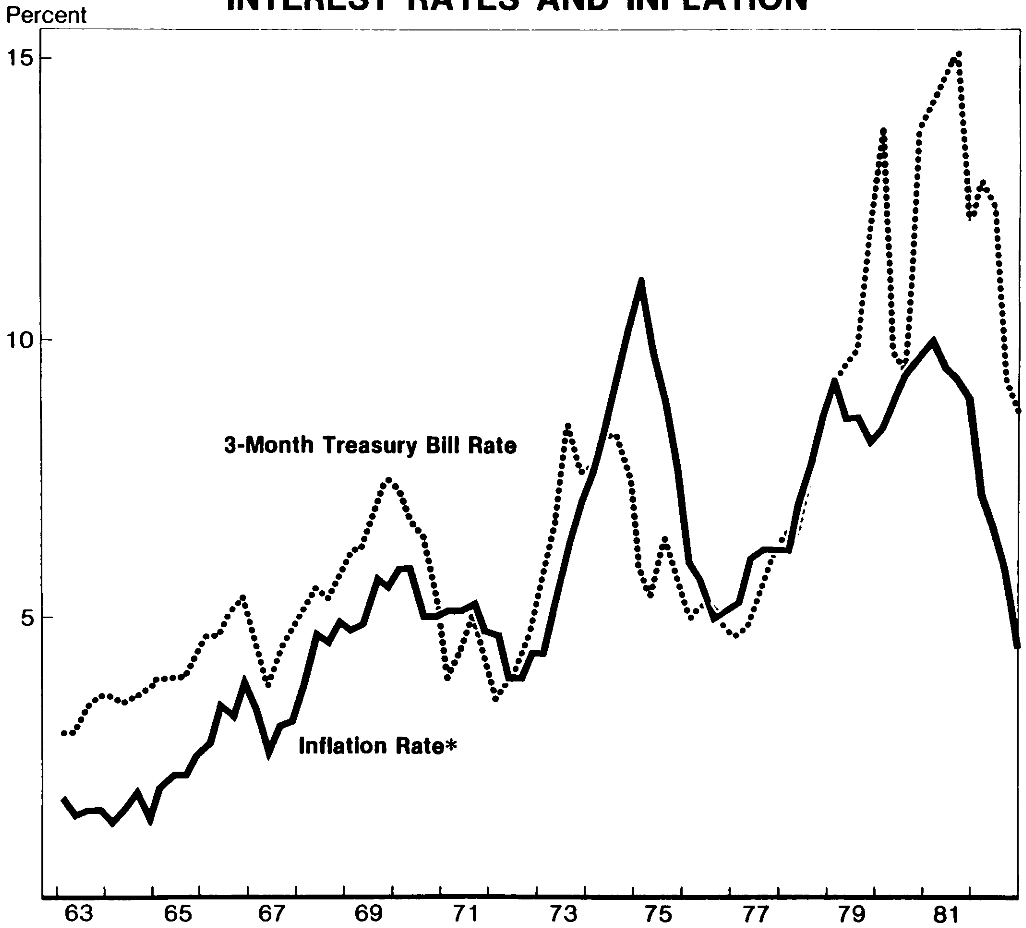


Chart III

INTEREST RATES AND INFLATION

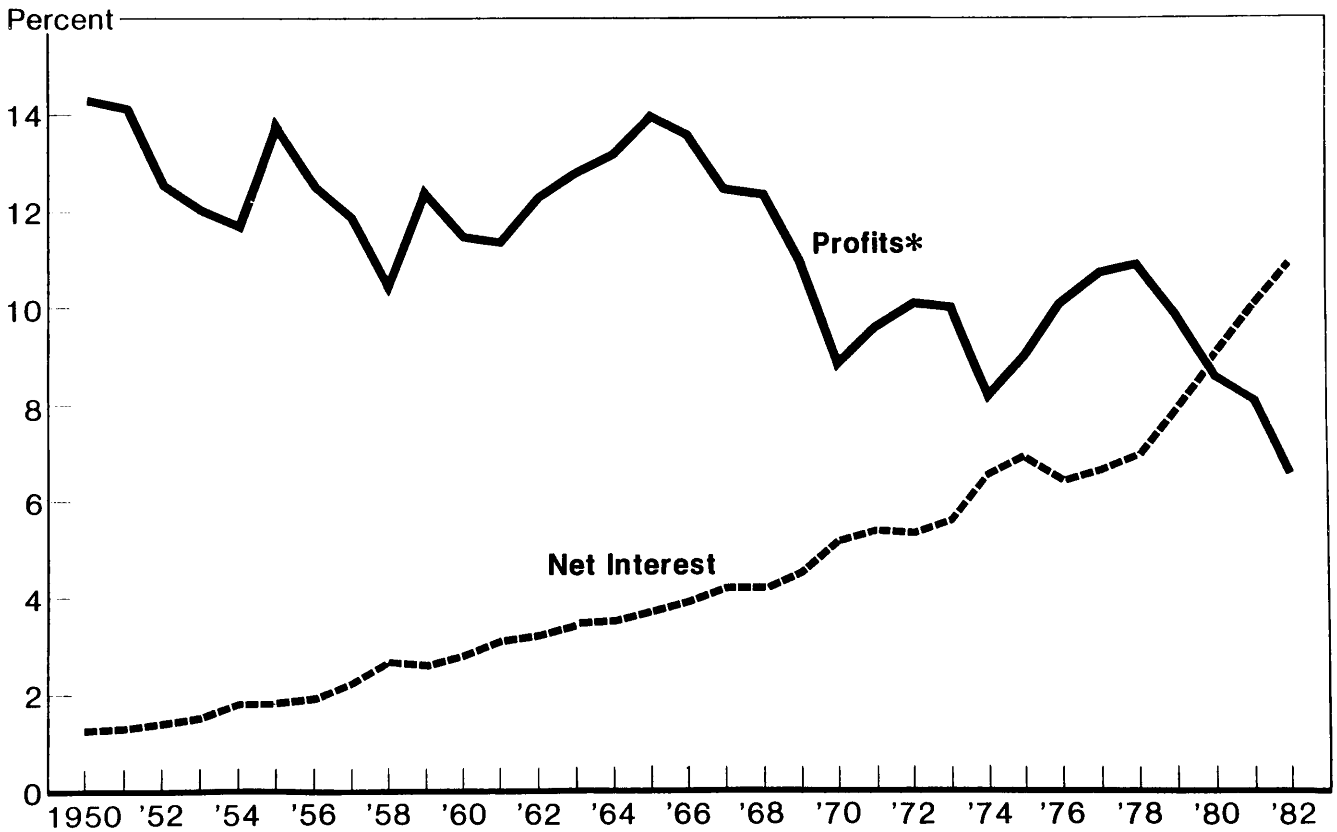


* Growth from year earlier in GNP deflator.
Plotted quarterly.

January 19, 1983 A28

Chart IV

PROFIT AND INTEREST SHARES OF NATIONAL INCOME

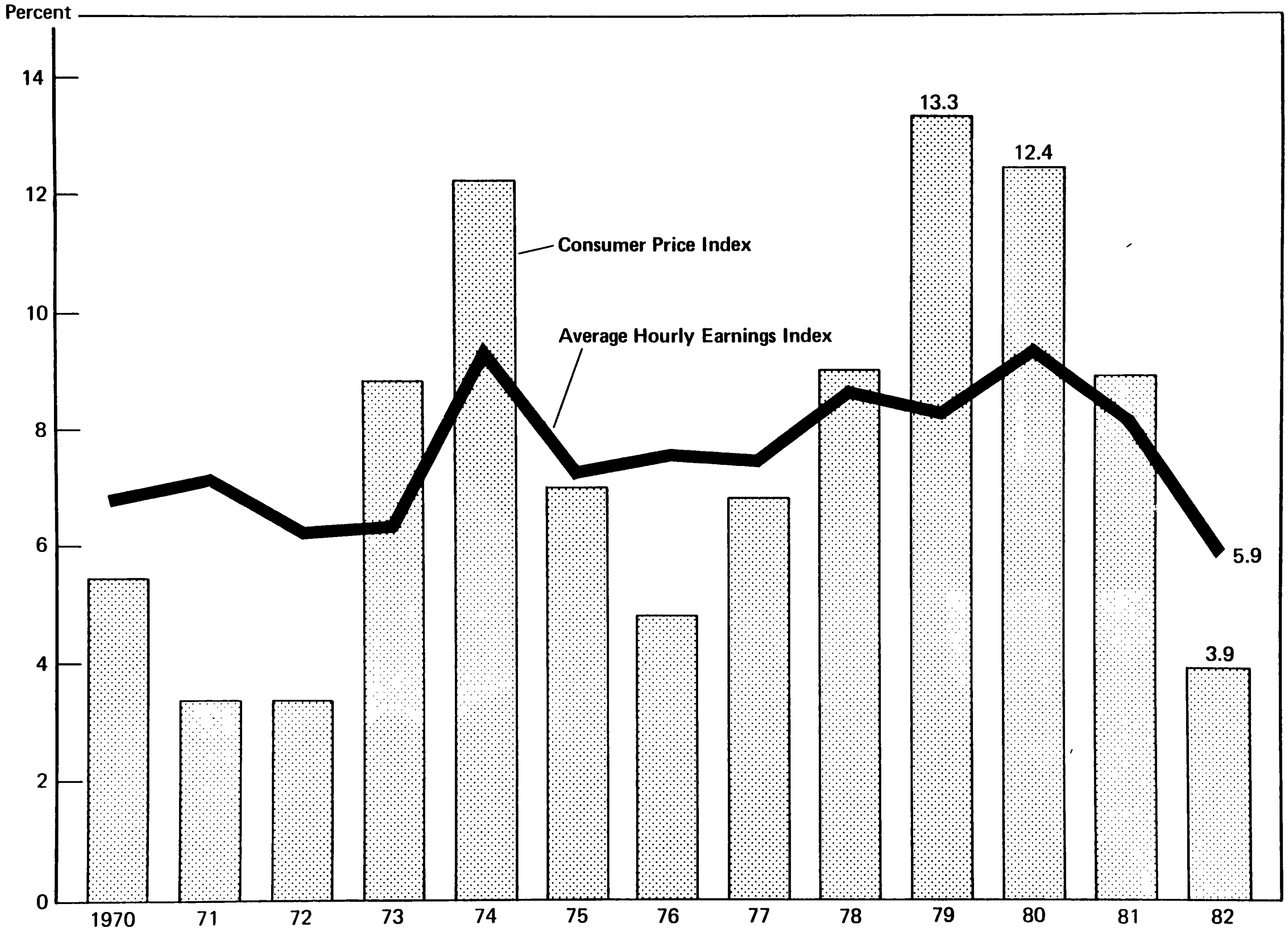


*Pretax corporate profits after allowance for depreciation and inventory profit.

Chart V

YEARLY GROWTH IN INFLATION AND WAGES

(Percent Change from December to December)

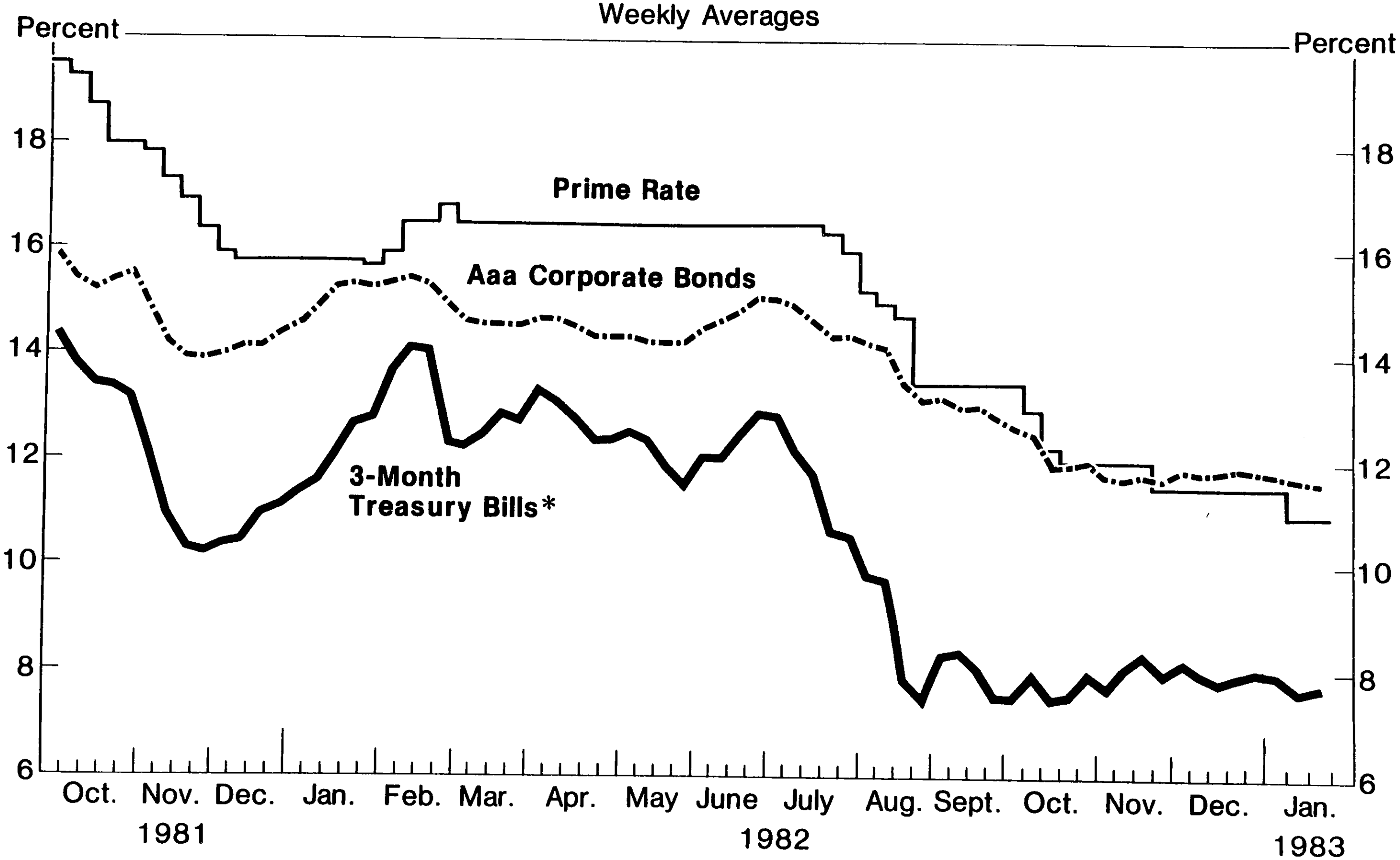


January 21, 1983-A209

Chart VI

INTEREST RATES

Weekly Averages



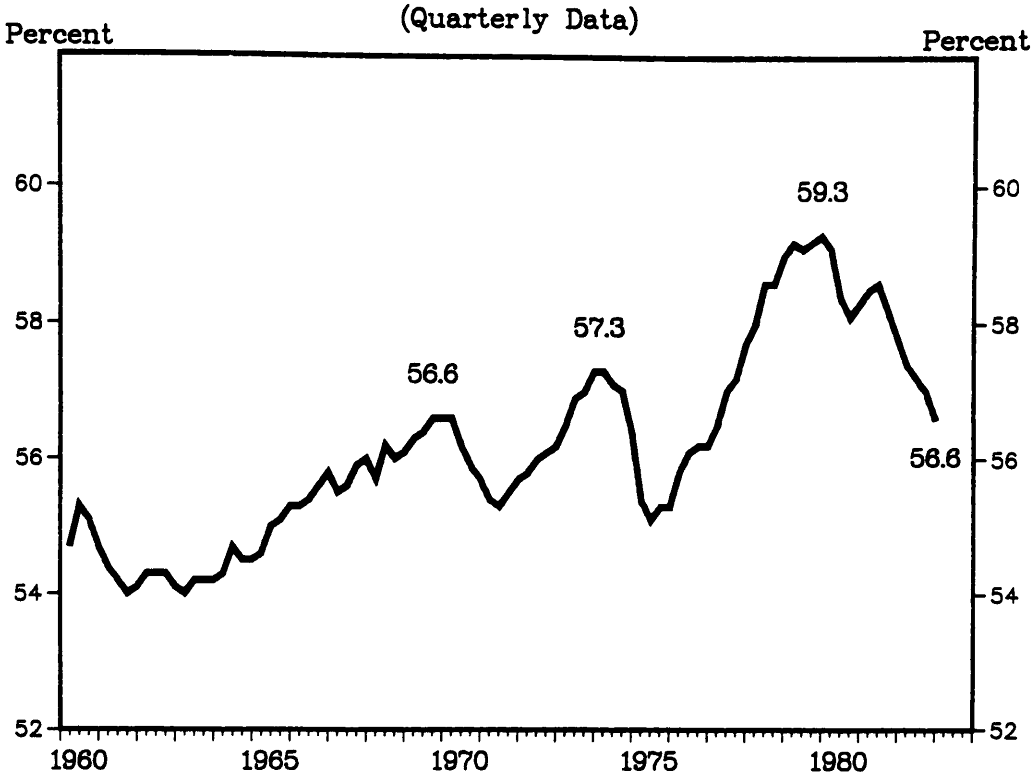
*Bank discount basis

January 24, 1983-A203

Chart VII

Employment Rate

(Quarterly Data)



Unemployment Rate

(Quarterly Data)

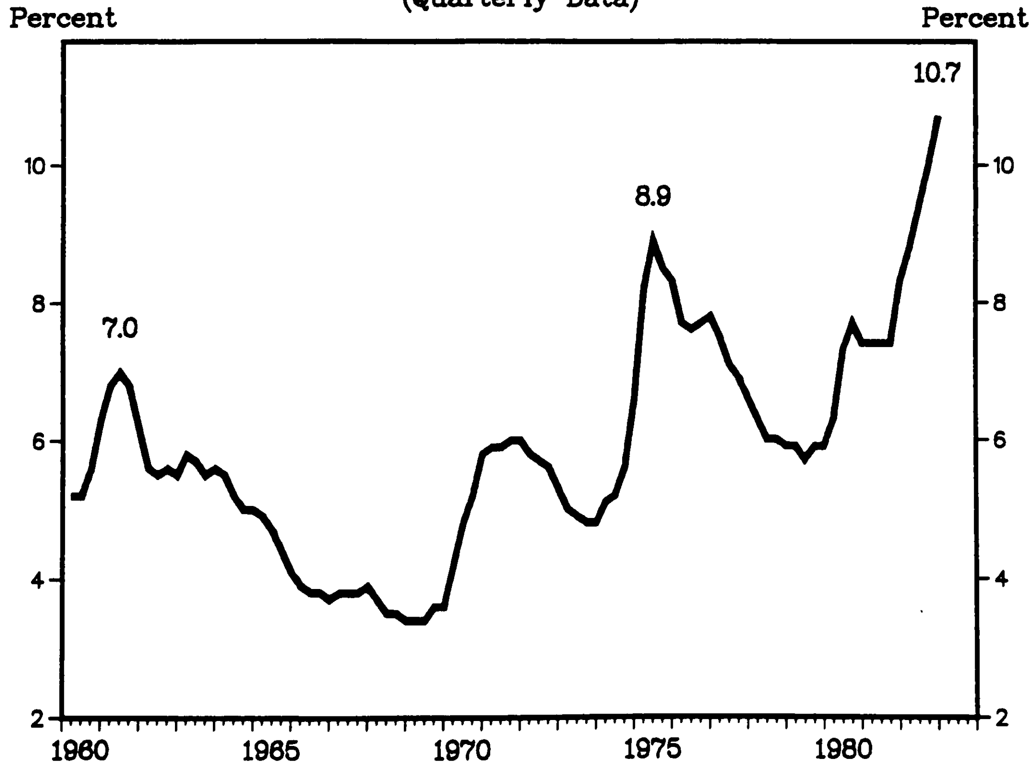
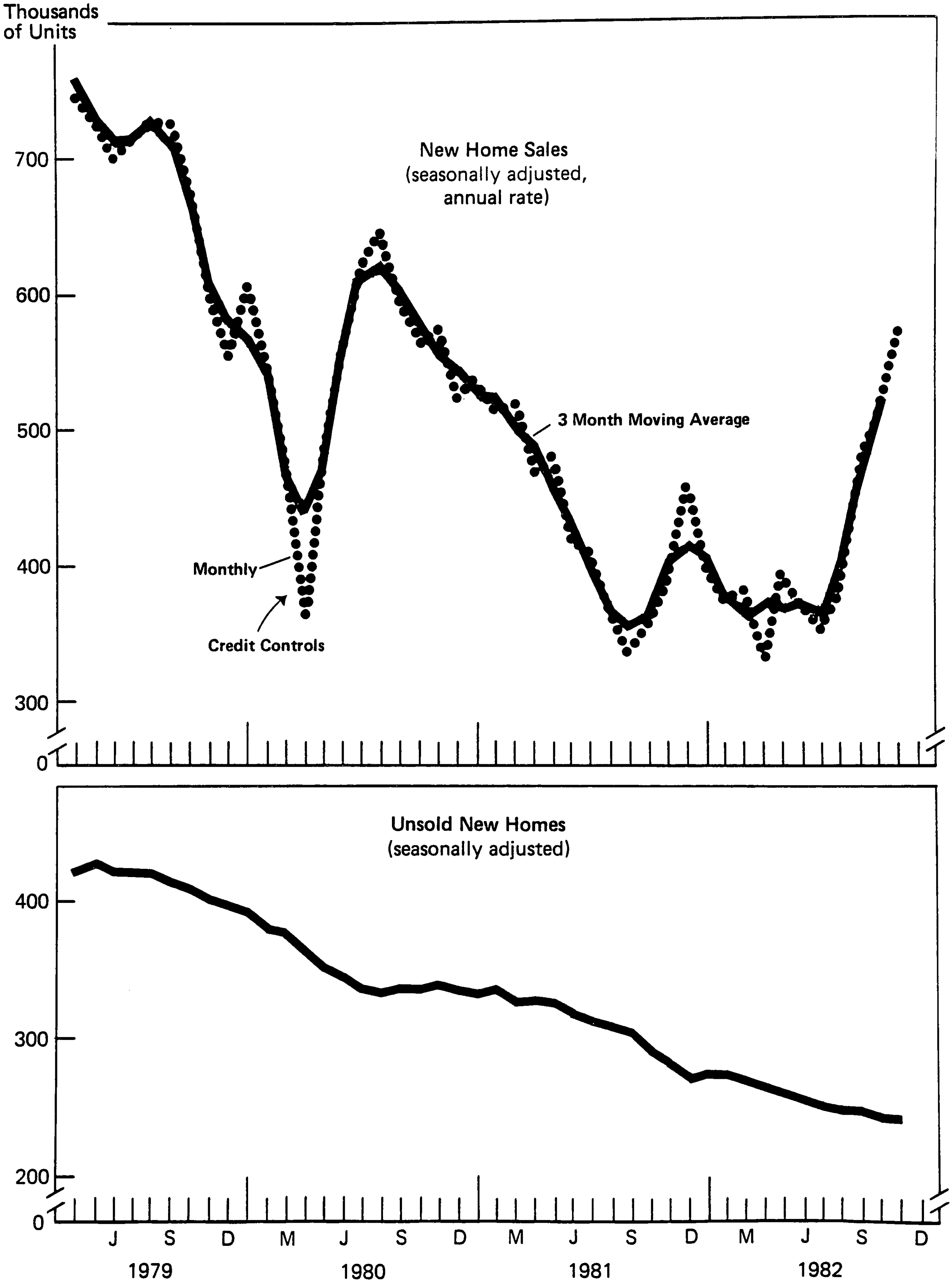


Chart VIII

NEW HOME SALES AND INVENTORIES OF UNSOLD HOUSES

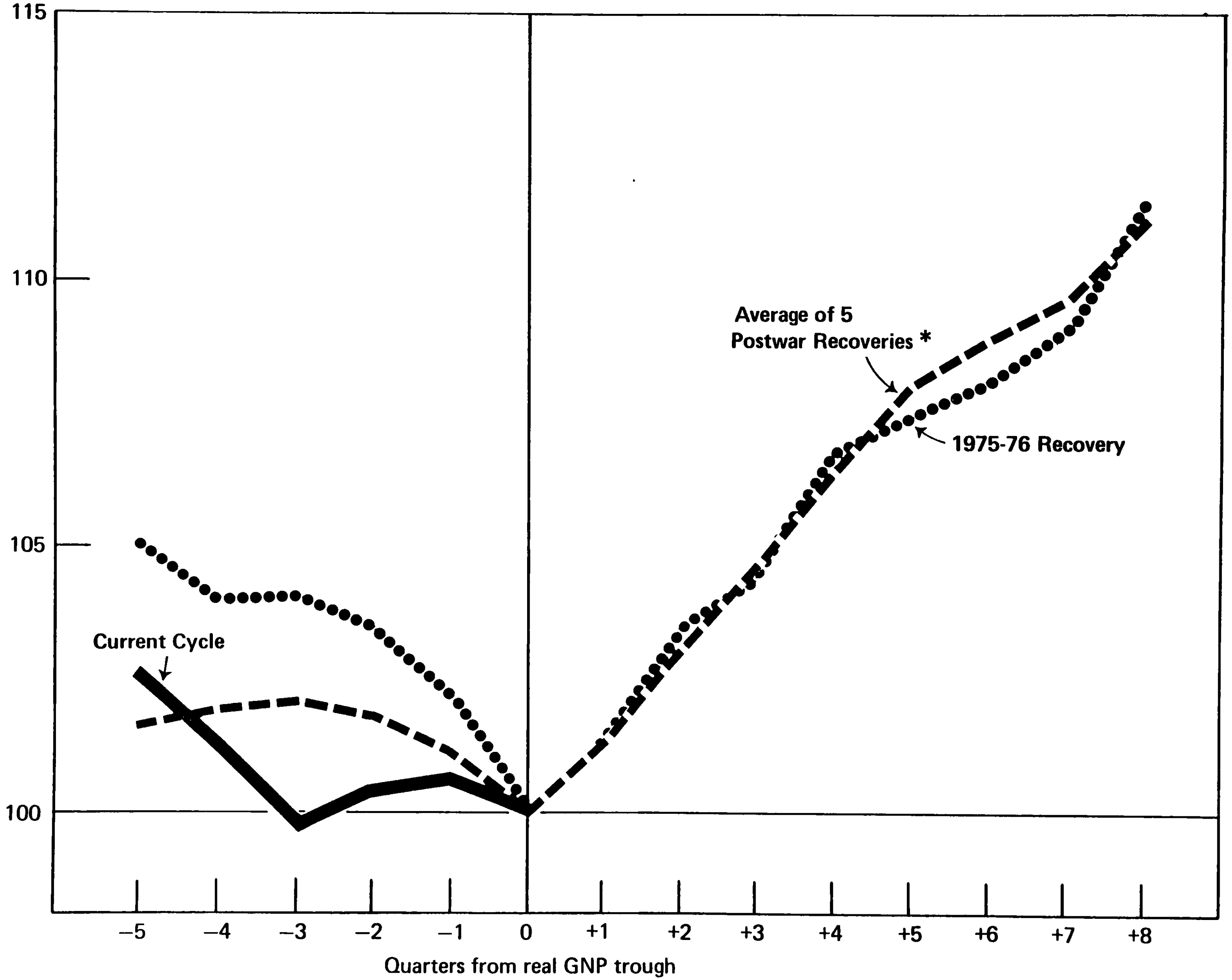


January 21, 1983-A212

Chart IX

THE PATH OF POSTWAR ECONOMIC RECOVERIES

Real GNP trough = 100

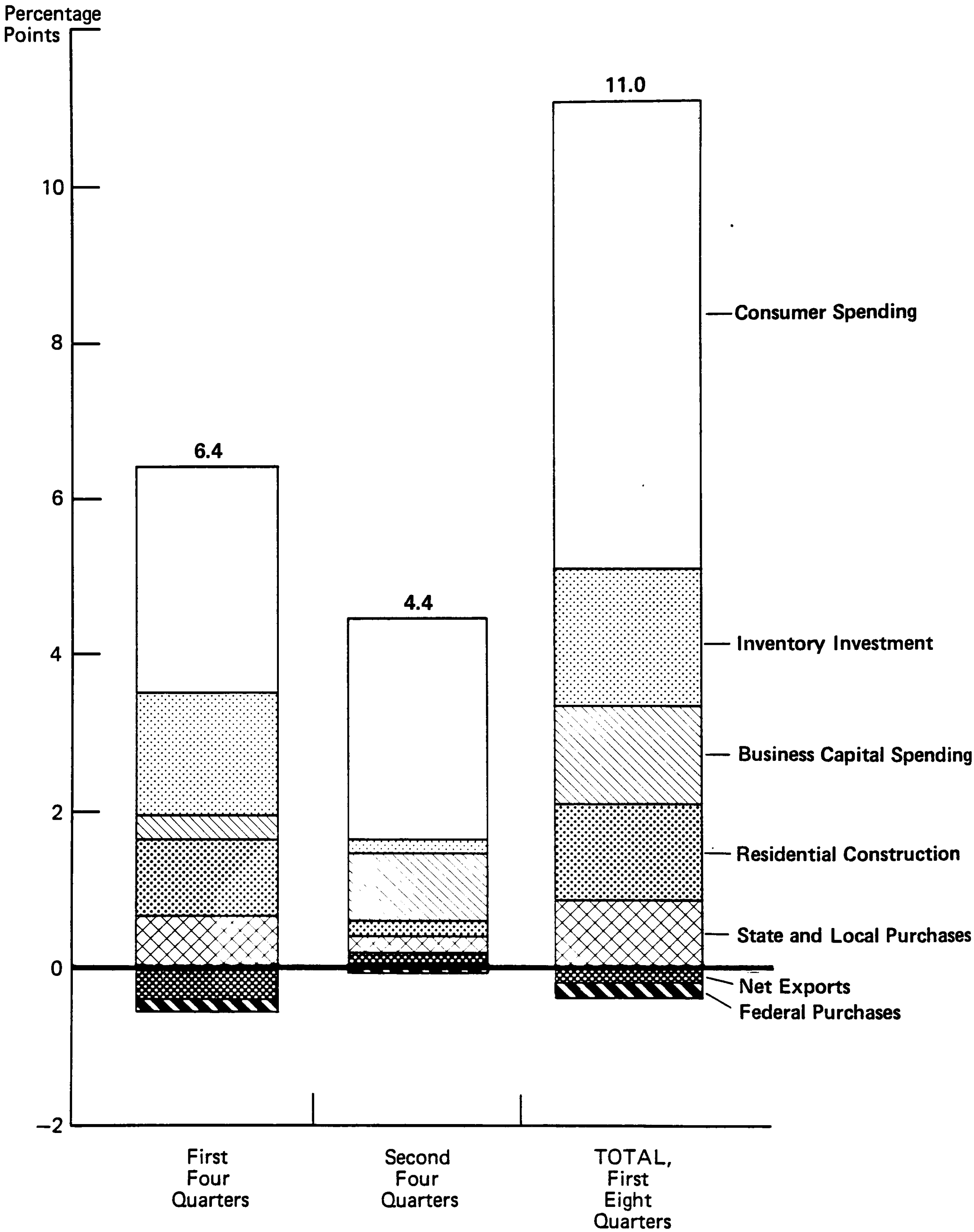


* Postwar recoveries excluding the Korean War period and the short-lived 1980-81 recovery.

January 21, 1983-A210

Chart X

CONTRIBUTIONS TO A TYPICAL RECOVERY*
BY REAL GNP COMPONENT

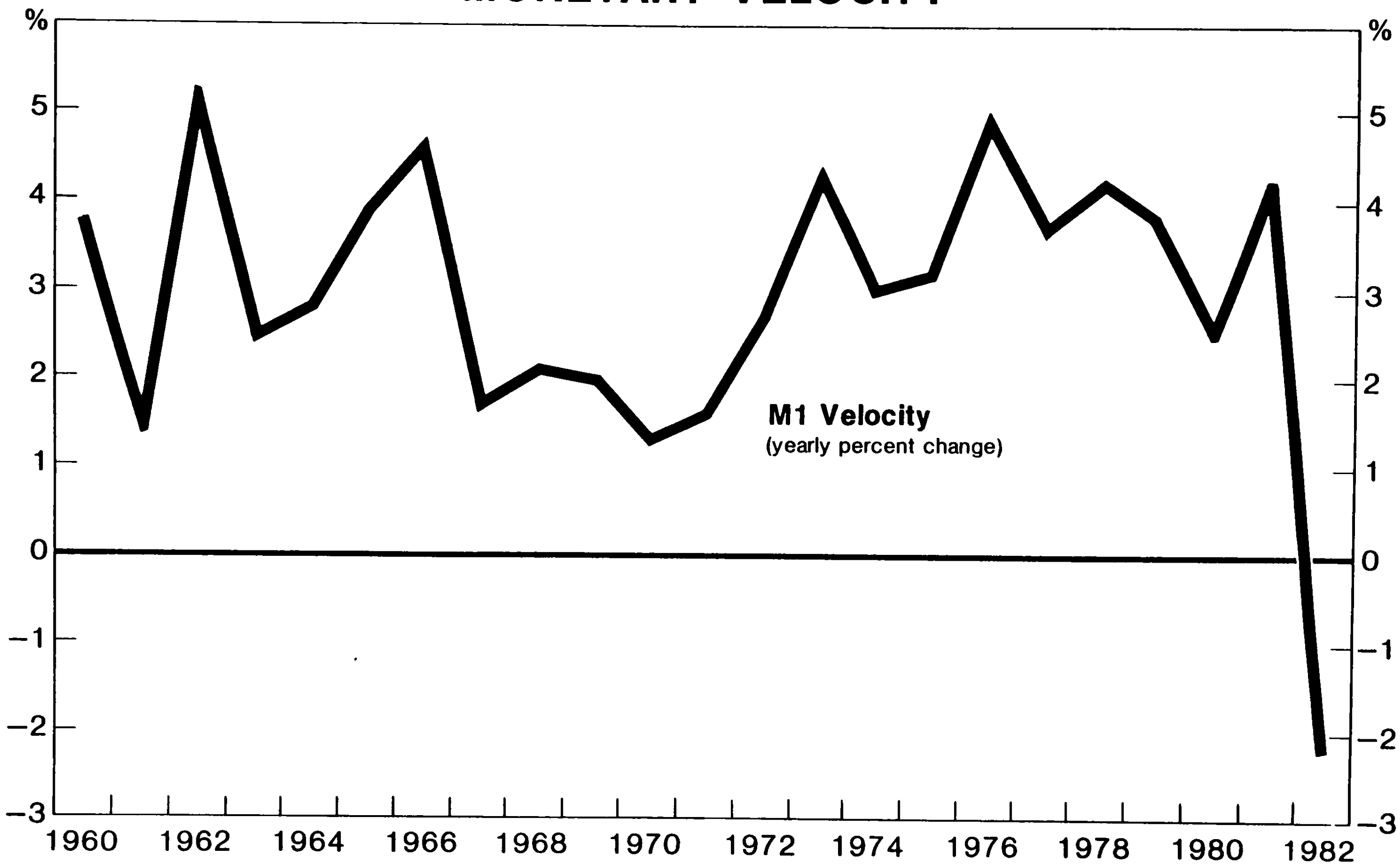


* Average of postwar recoveries, excluding the Korean War period and the short-lived 1980-81 recovery.

January 21, 1983-A213

Chart XI

MONETARY VELOCITY



January 12, 1983-A35

TREASURY NEWS

epartment of the Treasury • Washington, D.C. • Telephone 566-2041

January 26, 1983

FOR RELEASE WHEN AUTHORIZED AT PRESS CONFERENCE

TREASURY FEBRUARY QUARTERLY FINANCING

The Treasury will raise about $8,700 million of new cash and refund $5,769 million of securities maturing February 15, 1983, by issuing $6,500 million of 3-year notes, $4,500 million of 10-year notes, and $3,500 million of 29-3/4-year bonds. The $5,769 million of maturing securities are those held by the public, including $22 million held, as of today, by Federal Reserve Banks as agents for foreign and international monetary authorities.

The three issues totaling $14,500 million are being offered to the public, and any amounts tendered by Federal Reserve Banks as agents for foreign and international monetary authorities (including the $22 million of maturing securities) will be added to that amount.

In addition to the public holdings, Government accounts and Federal Reserve Banks, for their own accounts, hold $2,189 million of the maturing securities that may be refunded by issuing additional amounts of the new securities at the average prices of accepted competitive tenders.

Details about each of the new securities are given in the attached "highlights" of the offering and in the official offering circulars.

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Attachment

HIGHLIGHTS OF TREASURY
OFFERINGS TO THE PUBLIC
FEBRUARY 1983 FINANCING
TO BE ISSUED FEBRUARY 15, 1983

January 26, 1983

Amount Offered:			
To the public	$6,500 million	$4,500 million	$3,500 million
Description of Security:			
Term and type of security	3-year notes	10-year notes	29-3/4-year bonds
Series and CUSIP designation	Series L-1986 (CUSIP No. 912827 PC 0)	Series A-1993 (CUSIP No. 912827 PD 8)	Bonds of 2007-2012 (CUSIP No. 912810 DB 1)
Maturity date	February 15, 1986	February 15, 1993	November 15, 2012
Call date	No provision	No provision	November 15, 2007
Interest rate	To be determined based on the average of accepted bids	To be determined based on the average of accepted bids	10-3/8%
Investment yield	To be determined at auction	To be determined at auction	To be determined at auction
Premium or discount	To be determined after auction	To be determined after auction	To be determined after auction
Interest payment dates	August 15 and February 15	August 15 and February 15	May 15 and November 15
Minimum denomination available	$5,000	$1,000	$1,000
Terms of Sale:			
Method of sale	Yield Auction	Yield Auction	Yield Auction
Competitive tenders	Must be expressed as an annual yield, with two decimals, e.g., 7.10%	Must be expressed as an annual yield, with two decimals, e.g., 7.10%	Must be expressed as an annual yield, with two decimals, e.g., 7.10%
Noncompetitive tenders	Accepted in full at the average price up to $1,000,000	Accepted in full at the average price up to $1,000,000	Accepted in full at the average price up to $1,000,000
Accrued interest payable by investor	None	None	$26.36740 per $1,000 (from November 15, 1982, to February 15, 1983)
Payment by non-institutional investors	Full payment to be submitted with tender	Full payment to be submitted with tender	Full payment to be submitted with tender
Deposit guarantee by designated institutions	Acceptable	Acceptable	Acceptable
Key Dates:			
Deadline for receipt of tenders	Tuesday, February 1, 1983, by 1:30 p.m., EST	Wednesday, February 2, 1983, by 1:30 p.m., EST	Thursday, February 3, 1983, by 1:30 p.m., EST
Settlement date (final payment due from institutions)			
a) cash or Federal funds	Tuesday, February 15, 1983	Tuesday, February 15, 1983	Tuesday, February 15, 1983
b) readily collectible check	Friday, February 11, 1983	Friday, February 11, 1983	Friday, February 11, 1983

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE

January 31, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $6,001 million of 13-week bills and for $6,003 million of 26-week bills, both to be issued on February 3, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing May 5, 1983			:	26-week bills maturing August 4, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	97.957a/	8.082%	8.37%	:	95.869	8.171%	8.64%
Low	97.941	8.145%	8.43%	:	95.834	8.240%	8.72%
Average	97.947	8.122%	8.41%	:	95.842	8.225%2/	8.70%

a/ Excepting 1 tender of $2,000,000.

Tenders at the low price for the 13-week bills were allotted 80%.
Tenders at the low price for the 26-week bills were allotted 23%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 61,570	$ 60,570	:	$ 72,575	$ 37,575
New York	10,643,540	4,812,540	:	11,026,075	4,946,555
Philadelphia	36,535	36,535	:	42,200	17,200
Cleveland	68,130	48,130	:	150,590	62,090
Richmond	47,325	42,325	:	78,750	42,980
Atlanta	60,860	60,760	:	35,175	34,985
Chicago	919,190	399,490	:	951,860	214,650
St. Louis	40,905	39,805	:	44,655	38,885
Minneapolis	10,385	10,385	:	10,050	10,050
Kansas City	41,135	40,635	:	48,060	48,060
Dallas	32,090	32,090	:	19,685	19,685
San Francisco	796,290	151,290	:	819,385	249,385
Treasury	266,580	266,580	:	281,290	281,290
TOTALS	$13,024,535	$6,001,135	:	$13,580,350	$6,003,390
Type					
Competitive	$11,144,980	$4,271,580	:	$11,418,950	$3,991,990
Noncompetitive	1,034,995	1,034,995	:	737,900	737,900
Subtotal, Public	$12,179,975	$5,306,575	:	$12,156,850	$4,729,890
Federal Reserve	783,060	633,060	:	725,000	575,000
Foreign Official Institutions	61,500	61,500	:	698,500	698,500
TOTALS	$13,024,535	$6,001,135	:	$13,580,350	$6,003,390

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 7.967%.

R-2008

FOR IMMEDIATE RELEASE JANUARY 31, 1983

The Treasury announced today that the 2-1/2 year Treasury yield curve rate for the five business days ending January 31, 1983, averaged 9.70 % rounded to the nearest five basis points. Ceiling rates based on this rate will be in effect from Tuesday, February 1, 1983 through Monday, February 14, 1983.

Detailed rules as to the use of this rate in establishing the ceiling rates for small saver certificates were published in the Federal Register on July 17, 1981.

Small saver ceiling rates and related information is available from the DIDC on a recorded telephone message. The phone number is (202)566-3734.

Approved ____________________
Francis X. Cavanaugh, Director
Office of Government Finance
& Market Analysis

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TREASURY NEWS
partment of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
January 31, 1983

Contact: Charles Powers
(202)566-2041

TREASURY ANNOUNCES PUBLIC MEETING TO DISCUSS
US-SWEDEN TAX TREATY ISSUES, ON FEBRUARY 17, 1983

The Treasury Department today announced that it will hold a public meeting on February 17, 1983, to solicit the views of interested persons regarding issues being considered during negotiations of a new income tax treaty between the United States and Sweden.

The public meeting will be held at the Treasury Department, at 2:00 p.m., in room 4426. Persons interested in attending are requested to give notice in writing by February 10, 1983, of their intention to attend. Notices should be addressed to Steven R. Lainoff, Associate International Tax Counsel, Department of the Treasury, Washington, D.C. 20220.

Today's announcement of the February public meeting follows the conclusion of the second round of negotiations between representatives of the United States and Sweden to develop a new income tax treaty for the avoidance of double taxation and the prevention of tax evasion. The existing treaty between the United States and Sweden was signed in 1939.

The Treasury seeks the views of interested persons in regard to the full range of income tax treaty issues, as well as other matters that may have relevance to an income tax treaty between the United States and Sweden. The February 17 public meeting will provide an opportunity for an exchange of views, and will permit discussion of the United States position in regard to the issues presented.

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R-2009

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TREAS

FOR RELEASE UPON DELIVERY
EXPECTED AT 9:30 A.M.
Tuesday, February 1, 1983

TESTIMONY OF THE HONORABLE DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
HOUSE APPROPRIATIONS COMMITTEE

Mr. Chairman and Members of the Committee:

It is a pleasure to meet with you today and to discuss the Administration's 1984 budget proposals. The development of a sound fiscal policy was one of the central objectives of the Reagan Administration when it came into office two years ago. For too long a time Americans had watched the share of GNP accounted for by Federal spending and taxes move upward. As the government siphoned off resources from the private sector and the money supply expanded, economic activity stagnated and inflation soared.

In February 1980 the Administration put before Congress a four point plan to revitalize the economy. Our program included spending restraint, tax reductions, regulatory reform, and support of the Federal Reserve's efforts to attain gradual, steady reduction in the rate of monetary growth.

The transition to a noninflationary environment has been somewhat more difficult than anticipated. We have seen two years of serious economic recession as a result of the inflation/tax spiral.

However, the worst is now over. There has been clear progress on inflation, and consumer price growth has dropped dramatically from 12.4 percent in 1980 to 3.9 percent in 1982. Interest rates are down from peak levels of 21-1/2 percent on the prime in December 1980 to 11 percent currently, and the stock market last year made new highs. Indicators such as housing, inventories, and real income show the economy is poised for recovery. Alongside these favorable developments, there remains distressingly high unemployment.

The task now is to encourage the renewal of economic growth to reduce unemployment and provide productive job opportunities in the private sector. In so doing we must not repeat the errors of the past and return to an inflationary economy.

The current domestic situation is complicated by the existence of large Federal budget deficits and the threat of even larger ones in years to come. These budget deficits will have to be reduced, since their persistence would inevitably lead to very adverse consequences for the U.S. economy and its financial markets.

Many of the economic difficulties we face at home are also faced by countries abroad. The entire international economy is experiencing a severe slowdown, complicated by the special debt-servicing problems of a number of countries. My prepared statement today deals primarily with the U.S. domestic economy, but it is obvious that the domestic and international situations are closely linked. The clear need in both cases is to encourage expansion rather than undergo further contraction.

It is important to recognize that current difficulties are the culmination of a long period of deteriorating economic performance in this country. The U.S. economy was in deep trouble long before the current recession began. It follows that our policies must aim at lasting long-run solutions. There are no quick cures.

Inflation has led to a roughly parallel rise in key interest rates. As shown in Chart I on interest rates and inflation, the 3-month Treasury bill rate followed the rate of inflation very closely over most of the period from the early 1960's to present. Thus, inflation appears to have been a major factor in the increase in the bill rate during that time.

Rising rates of inflation after the mid-1960's did not lead to more rapid economic growth for any sustained period of time. Quite the contrary. Inflation and its inevitable consequence of higher interest rates finally choked off real growth altogether.

Approach of the Reagan Administration

The Administration's primary economic goal upon coming to office was a fundamental restructuring of the economy, including:

- bringing inflation under control;
- shifting the composition of activity away from government spending toward more productive endeavors in the private sector;
- providing an environment which would reward innovation, work effort, saving and investment, and in which free-market forces could operate effectively.

Over the past two years we have seen evidence that the Administration's program is working. The fundamental elements of recovery are now largely in place. Inflation has been brought under control. Interest rates are coming down, as shown in Chart II. Real wage growth is being restored. In addition, there have been other improvements -- notably in productivity growth and saving behavior -- which mark a shift away from the problems that contributed to sluggish economic performance in recent years.

Within this framework of very significant achievements, there remains the fact that the economy has been in recession and unemployment is high. The unemployment rate of 10.8 percent in December is, of course, a matter of great concern. The President has indicated in his State of the Union Message that he will be submitting special legislation to help deal with the problem.

The Current State of the Economy

The economy now stands poised for recovery. In fact, the recovery may well already be underway at this moment. It has been much longer in coming than we, or for that matter nearly all forecasters, had expected.

The delay occurred primarily because of the persistence of high interest rates and because of developments in the international sphere. On the international front, the economies of our leading trading partners continued to weaken. Weakness among all the industrialized nations was self-reinforcing. Furthermore, the financial difficulties of some of the newly industrializing nations had adverse impacts on economic activity here. These forces, combined with a general hesitancy on the part of the consumer, led to another round of inventory cutting in the second half of 1982 and delayed the expected turnaround of the economy.

Signals of an Economic Upturn

There are now clear signals that the economy is turning around and that the recession will soon be behind us. To summarize these signals:

- The index of leading indicators has risen for eight out of the last nine months.
- Housing is in the midst of a rapid recovery.
- Business trimmed inventories sharply in the final quarter of last year. Historically, a cleanout of inventories typically has been followed by a shift back to higher rates of production.
- Retail sales have begun to firm.
- Total industrial production stabilized in December and appears poised to turn upward.

The Typical Recovery

We would all hope for a vigorous recovery, not unlike those which occurred in the past. The typical postwar recovery path is shown in Chart III. Excluded from it are two atypical recoveries -- the first of which included the Korean War buildup and the second which got underway late in 1980 but was short-lived. The five recoveries contained in the average line in the chart were remarkably similar. Gains over the first eight quarters from the real GNP trough were within an extremely narrow range of 5 to 6 percent at an annual rate.

The contributions of GNP components to real growth during the typical recovery are shown in Chart IV. As it indicates, much of the initial thrust for expansion comes from:

- a resurgence in homebuilding activity, such as currently is underway;
- a swing in inventory investment from decumulation in the later stages of recession to accumulation; and
- a major contribution from consumer spending, with purchases of consumer durables registering particularly large increases.

By contrast, Federal spending normally declines as a share of GNP during recovery, and is not necessary for promoting expansion.

The Outlook for the Economy

A vigorous recovery of the type outlined would be most welcome. It would certainly help ease the Nation's budgetary problems. However, we recognize that the serious problems still confronting us may well hold growth during the next year or two below the typical recovery pattern.

- Our overall trade balance is likely to register further marked deterioration in the coming year.
- Real interest rates may persist at high levels, though remaining below those prevailing a year ago.
- The economy is in the process of undergoing marked structural change. Some of our industries may not quickly regain the vitality they experienced in the 1950's and 1960's. The shift of resources to emerging industries will take time.
- Most fundamentally, we are not yet fully out of the inflationary woods, and we cannot afford to direct monetary and fiscal policy toward excessively rapid economic expansion.

For these reasons, the Administration is forecasting fairly modest real growth at a 3.1 percent rate during the four quarters of 1983, rather than the typical recovery growth rate of about twice that much, though certainly we would welcome a stronger recovery. Growth is expected to pick up modestly to the 4 percent range in 1984 and the years beyond.

Policies for the Recovery

In setting policy for the remainder of the 1980's, we must recognize what we must not do. We no longer have the freedom of action to revert back to the overly stimulative monetary and fiscal policies pursued at times in the past, for these would surely lead to a resurgence of inflationary pressures and a new round of rising interest rates. Further, we must not reverse the fundamental tax restructuring put in place in 1981, for this was designed to provide the noninflationary incentives without which the private sector would continue to wither.

Policies for a Changing Economic Structure

For years private sector initiative and dynamic market forces have been stifled by unnecessary Federal regulation. It is important that we carry through with policies of reducing the regulatory burden on private industry. Noteworthy successes have been achieved in this area, particularly in the deregulation of the financial system. For the first time in the postwar period, small investors can count on being able to obtain market rates of return on their savings from banks and thrift institutions.

Further, we recognize that our economy and those of the other industrialized nations are undergoing a period of restructuring. This is an era of rapid technological change, and comparative advantage in the production of many goods and services is shifting from the already developed to the newly developing nations. Those nations which expend all their energies shoring up declining industries and resisting change will find themselves with industrial bases that are obsolete and with declining relative standards of living. Their more foresighted and innovative neighbors will be moving forward and capturing newly opening markets.

Government can ease the painful process of structural change within the economy. The President has announced a program that relies heavily on the market mechanism to deal with structural unemployment that stems from problems in both labor and product markets. This program will emphasize training, retraining and relocation, and job-search assistance for workers facing the lack or loss of jobs even after an economic recovery. Other proposals will be designed to reduce the barriers to youth employment.

Finally, in setting the proper course of policy for the 1980's, we must work closely with the other industrialized and newly industrializing nations of the world. Negotiations are nearing completion on measures to assure that the International Monetary Fund has adequate resources to help countries experiencing difficulties implement sound policies of economic adjustment. The negotiations are focusing in on an increase in IMF quotas to a new level in the range of $93-100 billion, representing an increase of 40-50 percent, and an expansion of the existing General Arrangement to Borrow (GAB) to a level of about $19 billion (from $7 billion). The participation of the United States in an increase in IMF resources is an essential complement to domestic measures to achieve sustainable economic growth and represents a valuable investment in defense of the economic interests of the American farmer, laborer, businessman, and consumer. The U.S. share of the increase in quotas and the GAB will be about $8 billion but will have no effect on net budget outlays or the budget deficit since simultaneous with any transfers to the IMF, the U.S. receives an offsetting increase in its international monetary reserve assets.

Legislation providing for the U.S. share of the increase in IMF resources will be submitted in the near future and I urge prompt approval by the Congress.

Monetary Policy

In addition to policies aimed at facilitating structural changes within the economy, we must maintain steady monetary and fiscal policies directed at reinvigorating economic activity. Steady, predictable money supply growth at a noninflationary pace has been, and continues to be, one of the major goals of the Administration's economic program. The Federal Reserve's efforts to achieve that goal have been complicated by a number of factors, such as far-reaching institutional changes in the banking and thrift industries. Nevertheless, the Fed has generally been successful, albeit in a somewhat erratic fashion.

Monetary policy faced a difficult and uncertain situation during much of the last year. Rapid institutional change in the form of new money market instruments blurred the boundaries between the various aggregates and made the achievement of any target rates of growth unusually difficult. There is also some indication that the recession may have led to an increased demand for liquidity and precautionary balances. In 1982, growth in monetary velocity -- the rate at which money is used -- turned negative for the first time in nearly three decades. Under the unusual economic and institutional circumstances of 1982, some temporary offset in the form of above-target rates of monetary growth was probably desirable.

The Federal Reserve's efforts to slow money growth have been accompanied by some volatile short-run swings. Growth in M1 was actually negative on a 13-week basis by mid-summer of last year, and then soared to the double-digit range by the end of the year. This recent acceleration has caused some observers to conclude that the fight against inflationary money growth has been abandoned. That is not true. Both the Administration and the Federal Reserve remain committed to the long-run goal of providing money growth at a noninflationary pace consistent with a steady and sustainable expansion of economic activity.

Fiscal Policy

The objectives of our fiscal policy upon coming to office two years ago were two-fold. First, we believed and still believe it was imperative to correct the disincentives to economic performance that had been built into the tax structure over the years. These disincentives arose in large measure, not by design, but through the interaction of a high rate of inflation with a progressive tax system and historical cost accounting of depreciable assets. Second, it was equally

imperative to reverse the seemingly inexorable growth of Federal spending, thereby freeing resources for use in the private sector. In moving to achieve these goals, we faced one major constraint, namely that our defense establishment had been allowed to deteriorate badly, so that our national survival mandated a stepped-up rate of defense spending.

The tax reforms that were put in place were designed primarily to restore an adequate rate of return for investment in plant and equipment and to put a halt to the steady ratcheting upward of marginal tax rates on labor and savings income. The investment incentives were necessary to bring long-depressed rates of business capital investment and productivity growth back up to acceptable standards. For individuals, the tax cuts were needed to protect incentives and purchasing power, and to keep American labor competitive in world markets. For the average taxpayer, they will only result in an actual dollar tax cut in 1983, after allowance for the effects of bracket creep and higher social security taxes. And that 1983 cut and tax indexing will be needed to offset bracket creep and increases in social security taxes scheduled to take effect in the future. These measures will greatly improve the competitive standing of American capital and labor in the world as economic recovery proceeds.

We were relatively successful in working with the Congress to achieve our goals of tax reform, but we were less successful in the area of outlay control. A major portion of the savings we had proposed in our original budget did not receive favorable action. This, along with much weaker economic activity than expected, has left us facing the prospect of large deficits even as the economy recovers.

The proposals in the FY-1984 Budget are directed at the crucial task of restoring noninflationary economic growth. This requires the preservation of the investment and work incentives provided by the tax reforms of 1981 and a reduction in the high deficits and interest rates which lie ahead unless corrective action is taken to bring government outlays under control.

The tax reforms already enacted will enable us to make good progress in rebuilding and modernizing America's plant and equipment as the recovery progresses. Incentives are in place to encourage saving and investment and to lower the cost of new machinery and structures. Taxes on American labor are coming down. These reforms will lead to a more productive, more competitive United States. The capital formation program will be financed by higher levels of personal saving, more generous capital consumption allowances, and higher retained earnings as profits recover from the current slump. These elements, plus state and local budget surpluses, form the Nation's savings pool.

Spending reduction will contribute to the recovery, and the recovery will contribute to deficit reduction. The deficit will fall as the economy advances, particularly if the recovery is a vigorous one. A strong recovery with 1-1/3 percent more real growth per year than in our forecast would bring the budget to near balance by 1988, provided we also curb the growth of Federal outlays.

However, if we fail to bring spending under control and if recovery is slow, we will face a deficit problem which is larger and longer-lasting than we can afford. In such case, the deficit could run in the range of 6 to 7 percent of GNP each year through 1988. Our tax reforms were designed to raise the private savings share, but still we would face the possibility of draining off a large part of the pool of savings, leaving less available for new capital formation. Interest rates could remain high, and the recovery could stall.

This Administration is determined that deficits of such magnitudes will not come to pass. We came to office with a program of boosting the rate of capital investment in order to place the economy on a faster growth track, and we will not allow ourselves to be diverted from that goal. We will take whatever measures are necessary to narrow the deficit to acceptable levels.

- Preferably, all of the necessary narrowing of the deficit would come from the outlay side. Total Federal spending represents the amount of resources absorbed by the government at the expense of the private sector. This spending can be financed by both taxes and borrowing, which in either case amounts to a drain on private resources. Only through spending reduction will the credit market find itself in a more favorable position.

- In the event that the combination of economic growth and outlay reductions is not sufficient to narrow the deficit to acceptable levels in the outyears, we are prepared to request additional revenue raising measures in those years. If the Congress chooses not to reduce spending, as we wish, then it is preferable to have the full cost of federal spending programs explicitly identified for the taxpayers who bear the burden of financing government. If additional revenues are needed, this Administration will do its best to structure the tax code in a way that minimizes disincentives for productive effort.

Our Budget Proposals

Spending reduction is crucial. Unfortunately, it has been difficult to achieve because of the built-in momentum of Federal spending programs. Consequently, we are proposing strong medicine. None of us will find it agreeable, but it is critical to the restoration of vitality to our economy. In prescribing the medicine, there must be assurance all will be willing to take the proper dosage, just as all of us will share in the benefits of a revitalized recovery. We, like a great many other nations in the world, have tried to live beyond our means. Now we must bring our spending into line with our productive capacity and strengthen the private sector which produces our national wealth.

The deficit reduction program that we propose contains four basic elements.

- The first is a freeze on 1984 outlays to the extent possible. Total outlays shall be frozen in real terms in 1984. The 6-month freeze on COLAs, as recommended by the Social Security Commission, is to be extended to other indexed programs. There will be a 1-year freeze on pay and retirement of Federal workers, both civilian and military. Many workers in the private sector have accepted freezes in their pay. Federal workers can also make a sacrifice, which hopefully will serve as an example for sectors of the economy which have not yet recognized the need for moderation in wage demands. As a final item of freeze, outlays for a broad range of nonentitlement programs will be held at 1983 levels.

- The second element of our budgetary program contains measures to control the so-called "uncontrollables." Laws have been so written that Federal payments are automatic to all those declared eligible. We plan a careful review of all such programs, taking special care to protect those truly in need.

- The third element is a cutback of $55 billion in defense outlays from original plans.

- Fourth is a set of proposals involving the revenue side of the budget, described below.

We are projecting receipts for the current year (fiscal year 1983) of $597.5 billion. For fiscal year 1984 we expect receipts to be $659.7 billion. The 1983 figure represents a decline of $20.3 billion from the fiscal year 1982 total of $617.8 billion. This decline, and indeed the absence of an increase in receipts in the range of $50-70 billion, is explained primarily by the recession. As I have already explained, our economic projections throughout the remainder of the recovery period are cautious. If real GNP grows at a faster rate than we have projected, then receipts for the current fiscal year, as well as for subsequent years, will be somewhat higher than we are now projecting.

In 1984, as the recovery is well underway, receipts are expected to rise to $659.7 billion, an increase over 1983 of $62.2 billion, representing an annual growth of 10.4 percent. This will occur as profit margins recover and other income shares continue to grow.

For the other years in our forecast period (1985-1988) we project an average annual growth rate of receipts about 10 percent without contingency taxes (and 11 percent per year including contingency taxes), with receipts reaching the $1 trillion mark for the first time in fiscal year 1988. All of these projections assume the legislative proposals included in the President's Fiscal Year 1984 Budget. Receipts under existing legislation will also grow, but at a somewhat lower 9-1/2 percent annual average rate.

It is noteworthy that individual income tax receipts will continue to rise over the 1985-1988 period, but only as <u>real</u> income rises. Beginning in 1985, we will no longer collect hidden taxes in the form of bracket creep caused by inflation. Without the indexation provision of ERTA, individuals would pay $6 billion more in taxes during fiscal year 1985 alone, and about $100 billion more during the entire forecast period -- 1985 through 1988.

There has been a gradual upward trend in unified budget receipts as a percent of GNP, shown in the top line of Chart V. As shown in the bottom line of the chart, a major shift in the composition of receipts has been the rising share of social insurance and other payroll taxes to fund social security and other retirement benefits.

There is no proposed omnibus tax bill in the President's budget message. However, there are several separate tax items. Proposed tax legislation in the President's budget can be conveniently grouped under three broad headings: Proposals that improve the income security of Americans, proposals that will improve our ability to produce future output, and, as an insurance policy, a contingency or standby tax, which is intended as a clear signal that we will not permit spending to increase in the outyears unless we pay for it up front.

In the first category, our principal recommendation is for adoption of the bipartisan social security proposals. These proposals, which will increase receipts to the social security funds by $9.8 billion in fiscal year 1984, $11.6 billion in 1985, and $10.6 billion in 1986, are necessary to insure the solvency and security of these trust funds.

The second category, proposals to improve the utilization of our human resources, includes the tuition tax credit, the exclusion of earnings on savings for higher education, the jobs tax credit for hiring the long-term unemployed, and the enterprise zone tax incentives. These will all improve our production capacity, either through increased investments in education or, more directly, by getting our currently underutilized force of experienced workers back to work. As a group, these proposals will reduce taxes $0.5 billion in 1984, $1.2 billion in 1985, and $1.7 billion in 1986.

Finally, the President has proposed a contingency tax plan designed to raise revenues of about 1 percent of GNP in the event that, after Congress has adopted the spending reduction proposals, there is insufficient economic growth to reduce the deficit below 2-1/2 percent of GNP. The contingency tax plan would not go into effect on October 1, 1985, unless the economy is growing on July 1, 1985. The contingency tax plan is an insurance program. It is important to have a plan in place so that the country and the world know that we will not tolerate a string of deficits that would exceed 2-1/2 percent of GNP. Chart VI shows the effect on the deficit that the contingency tax would have if it were implemented. It also shows how the budget picture would be altered by the stronger expansion that some private forecasters expect. The deficit path under high growth reflects the assumption that real GNP increases 1-1/3 percentage points faster than in the official forecast path, starting with FY-1983. Such growth would be in line with the performance from the end of 1960 to late 1966.

The contingency tax plan would contain two elements, each raising about half of the revenues that may be required. One element would be a temporary surcharge of 5 percent on individuals and corporations. The other element would be a temporary excise tax on domestically produced and imported oil designed to raise revenues of about $5 per barrel. The contingency tax alternative shown in the budget raises $146 billion over the 36-month period beginning October 1, 1985. The specific contingency tax plan we will be sending to Congress for adoption this year will be designed to raise revenues of about $130-150 billion over a temporary period of up to 36 months.

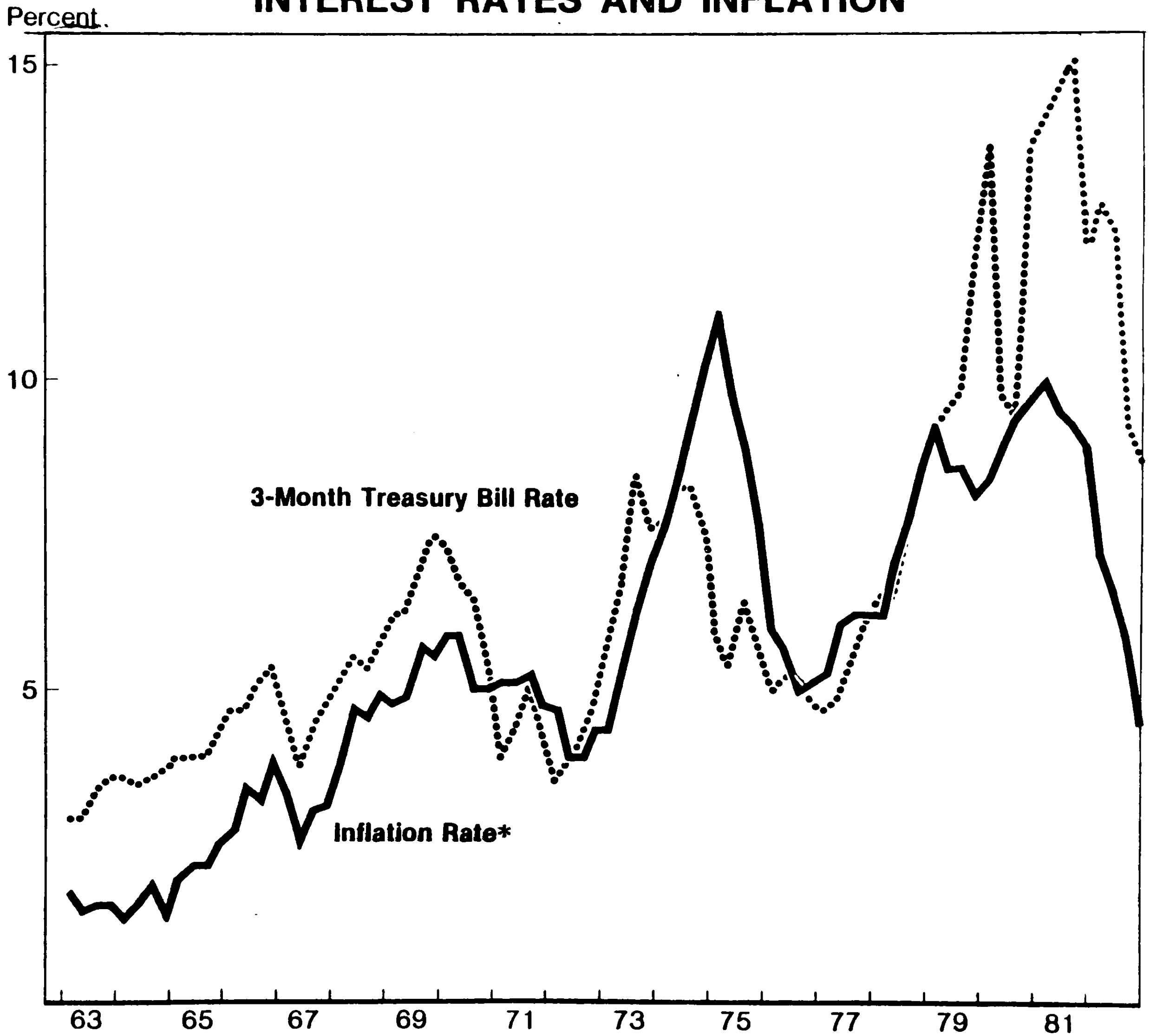
If these budget saving proposals are enacted, we will reduce the projected deficits by a total of $580 billion over the next five years, or by $2,400 for every man, woman, and child in the United States. The deficit as a share of GNP will be down to about 2-1/2 percent in 1988 from the 6-1/2 percent we expect this year. Total outlays will grow by only 7 percent per year in nominal terms over the next five years, compared with a bloated 13 percent between 1977 and 1981.

In addition, as part of our overall program, over the next year we will be taking a careful look at the entire structure of our tax system. We will be searching for ways to simplify the tax code and make it fairer while at the same time promoting economic growth by enhancing incentives for work effort, saving, and investment. This is the true road for putting people back to work and bringing the budget into balance.

We are confident that the deficit reduction program contained in this realistic budget is the right program for the economy at this critical juncture. The most important signals we can send the economy are spending restraint, deficit restraint, and a commitment to non-inflationary economic growth throughout the decade. This is the program we have devised. Together with the Congress, we can make it work.

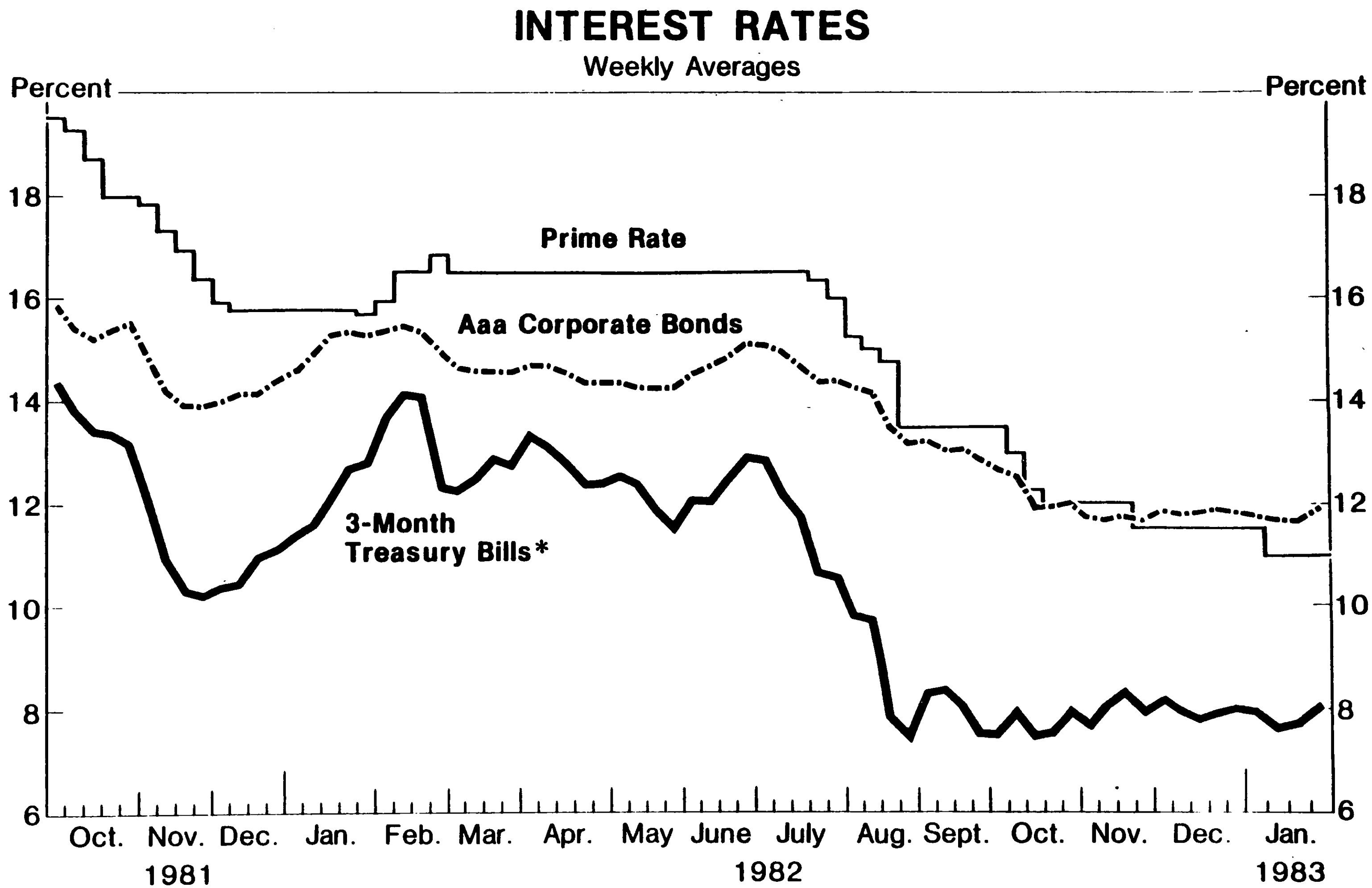
Chart I

INTEREST RATES AND INFLATION



* Growth from year earlier in GNP deflator.
Plotted quarterly.

Chart II



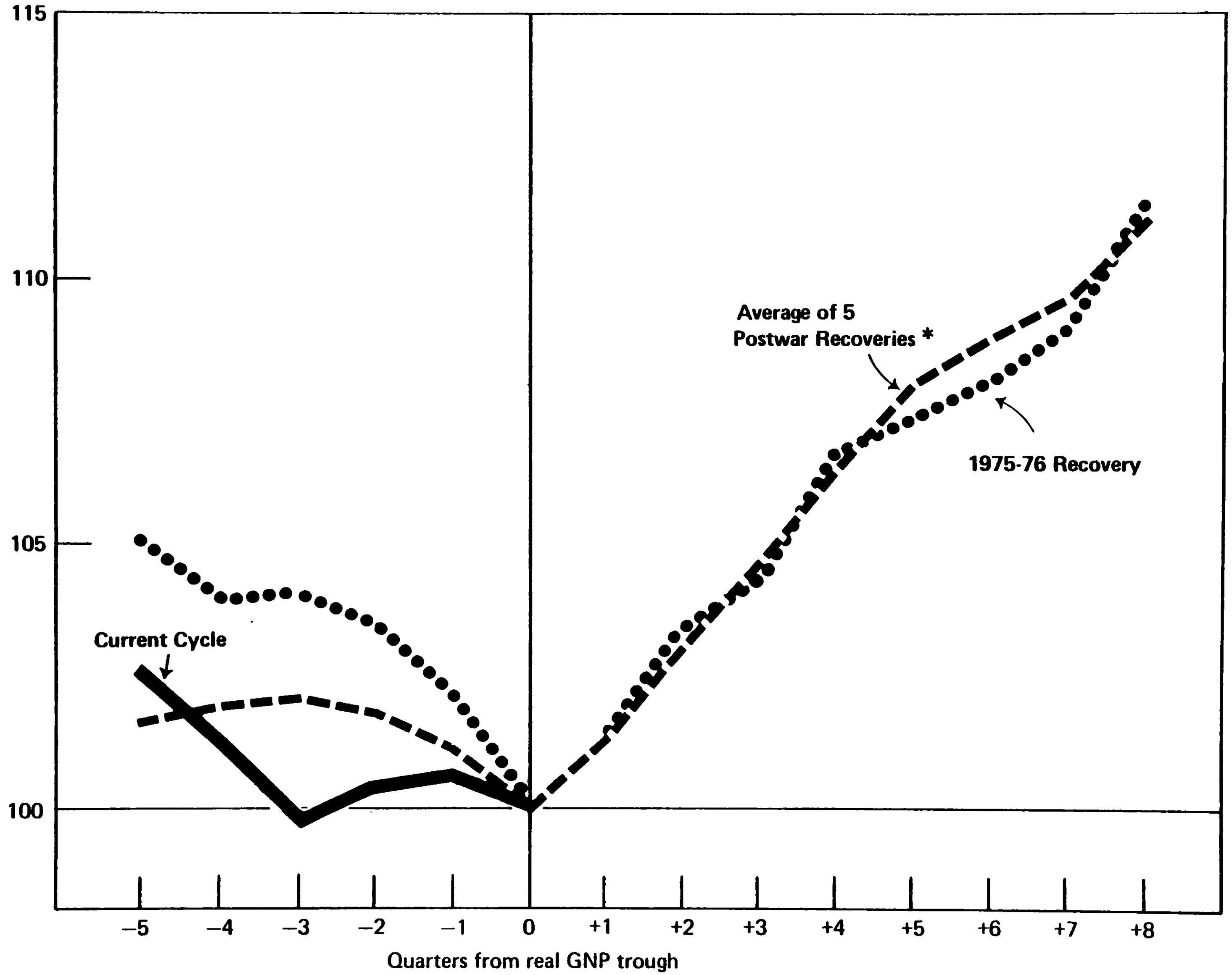
*Bank discount basis

January 31, 1983-A203

Chart III

THE PATH OF POSTWAR ECONOMIC RECOVERIES

Real GNP trough = 100

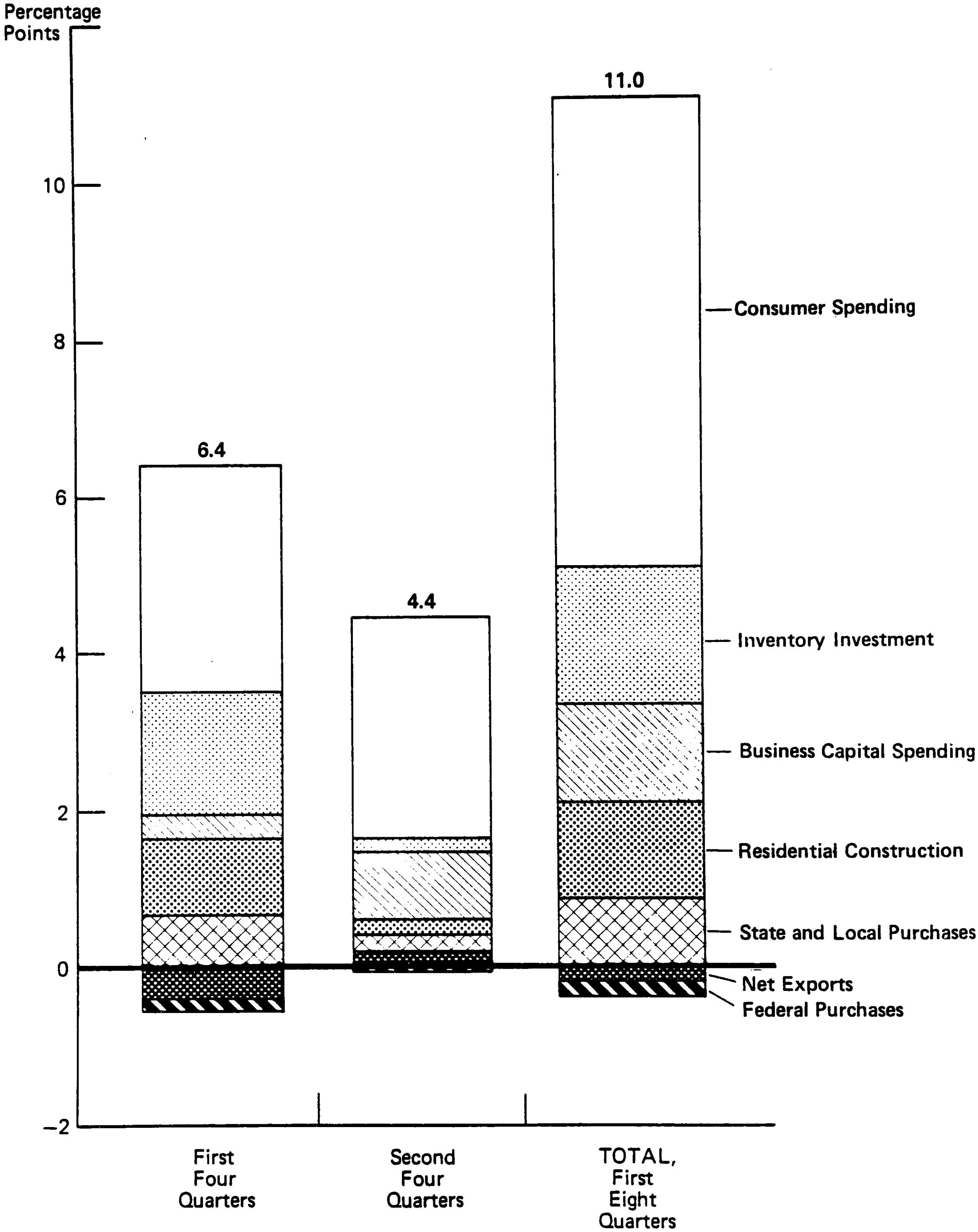


* Postwar recoveries excluding the Korean War period and the short-lived 1980-81 recovery.

January 25, 1983-A210

Chart IV

CONTRIBUTIONS TO A TYPICAL RECOVERY* BY REAL GNP COMPONENT



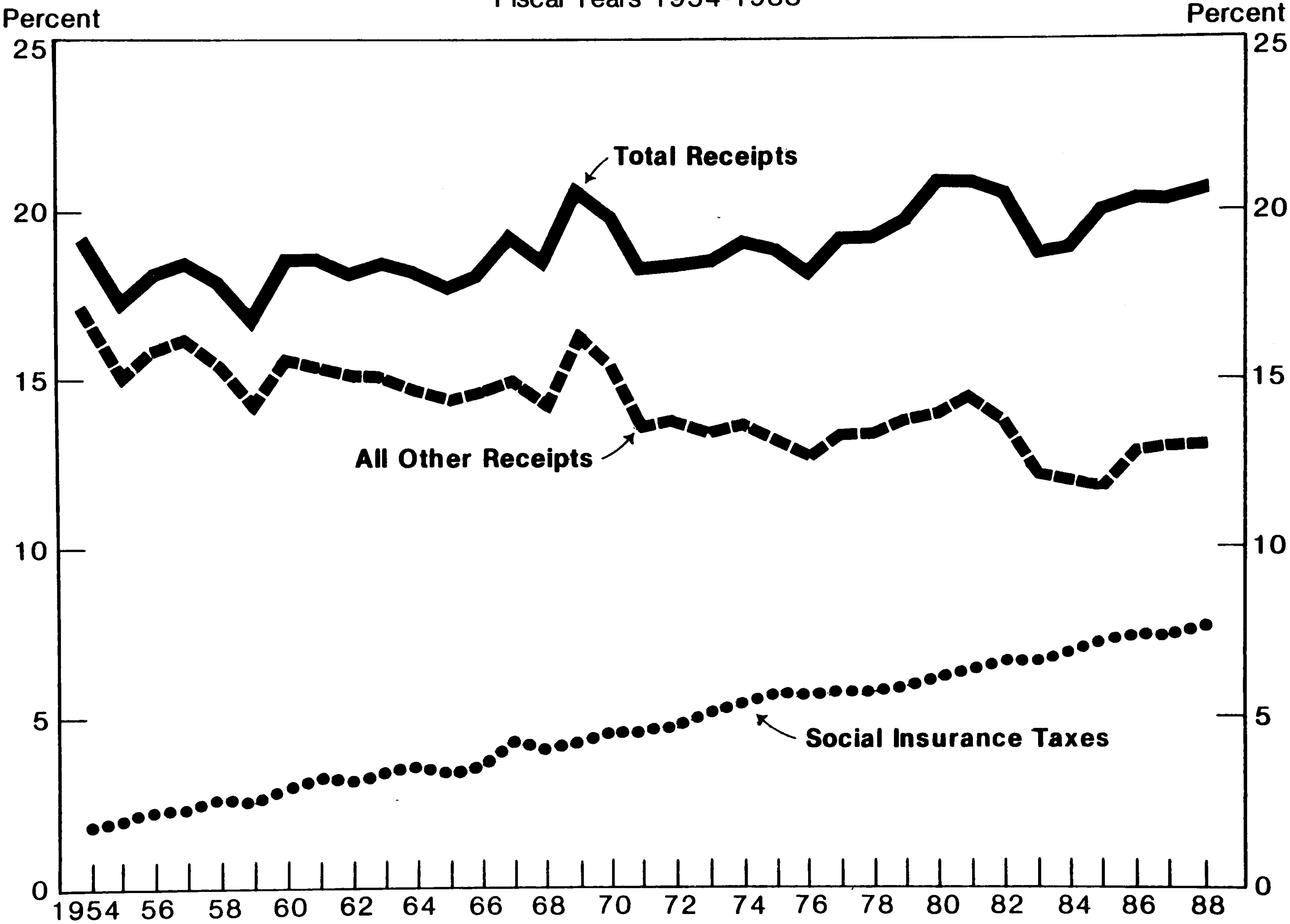
* Average of postwar recoveries, excluding the Korean War period and the short-lived 1980-81 recovery.

January 21, 1983-A213

Chart V

UNIFIED BUDGET RECEIPTS AS A PERCENT OF GNP *

Fiscal Years 1954-1988

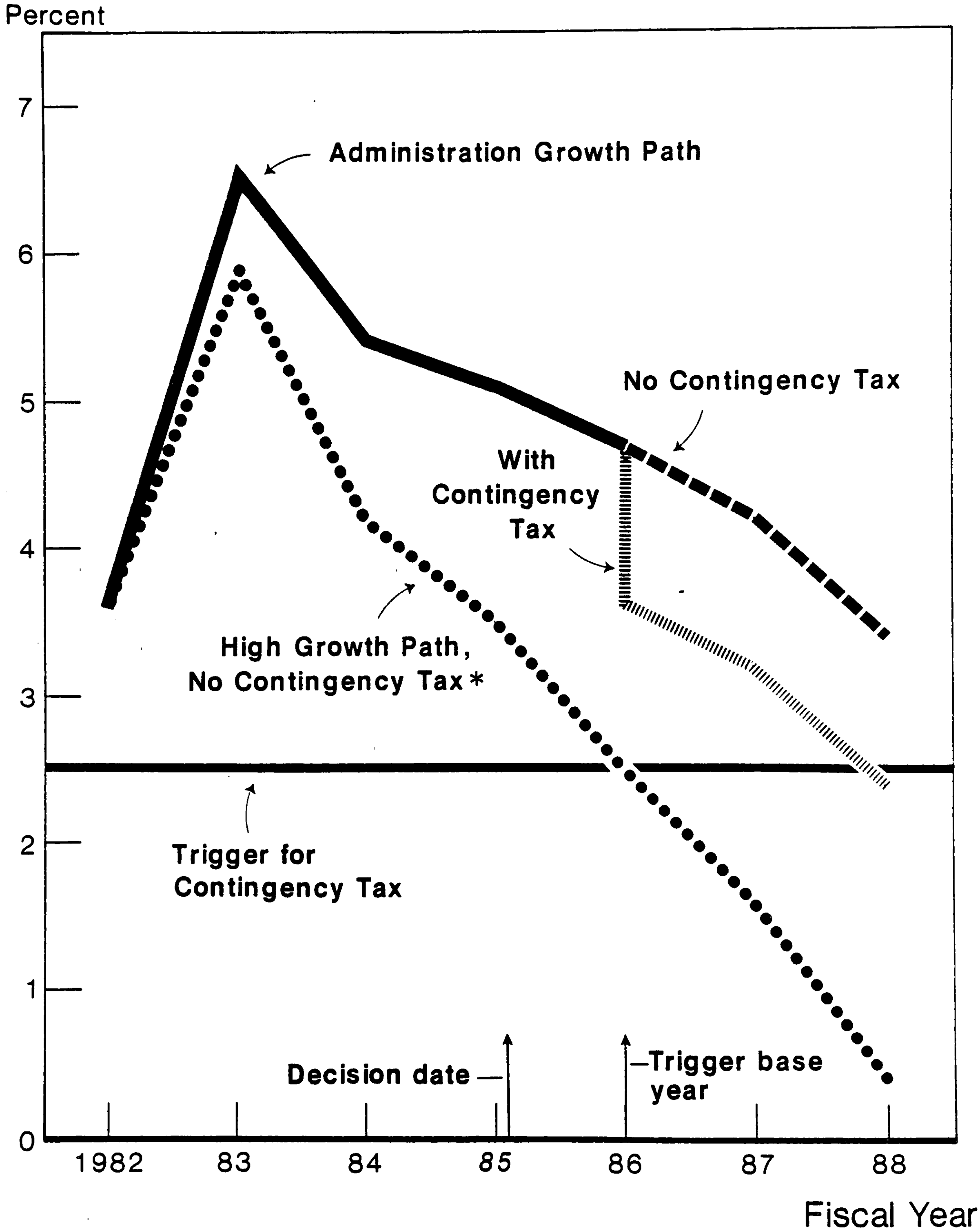


* Receipts include contingency taxes.

January 28, 1983-A215

Chart VI

THE DEFICIT AS A SHARE OF GNP



*Higher growth than the official path by 1-1/3 percentage point starting fiscal year 1983.

January 28, 1983-A214

TREASURY NEWS
epartment of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M.

February 1, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $ 12,000 million, to be issued February 10, 1983. This offering will provide $ 850 million of new cash for the Treasury, as the maturing bills are outstanding in the amount of $11,162 million, including $ 1,058 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and $ 2,058 million currently held by Federal Reserve Banks for their own account. The two series offered are as follows:

91-day bills (to maturity date) for approximately $ 6,000 million, representing an additional amount of bills dated November 12, 1982, and to mature May 12, 1983 (CUSIP No. 912794 CU 6), currently outstanding in the amount of $ 5,632 million, the additional and original bills to be freely interchangeable.

182-day bills (to maturity date) for approximately $ 6,000 million, representing an additional amount of bills dated August 12, 1982, and to mature August 11, 1983 (CUSIP No. 912794 DB 7), currently outstanding in the amount of $ 6,262 million, the additional and original bills to be freely interchangeable.

Both series of bills will be issued for cash and in exchange for Treasury bills maturing February 10, 1983. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

R-2011

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, February 7, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on February 10, 1983, in cash or other immediately-available funds or in Treasury bills maturing February 10, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS
epartment of the Treasury • Washington, D.C. • Telephone 566-2041

STATEMENT BY DONALD T. REGAN
SECRETARY OF THE TREASURY
AT A BUDGET BRIEFING
MONDAY, JANUARY 31, 1983
WASHINGTON, D.C.

Today we present the Fiscal 1984 budget and it carries a stern message: we must harness federal spending and reduce deficits.

This budget reflects a lot of hard work and difficult decisions. I believe it provides a realistic assessment of the economy and the role of government in our lives. We have been cautious in our outlook and careful in our approach.

Our forecasts are modest. They reflect a prudent examination of the economic forces at work in the country today. And they are in line with most private forecasts. The result is a sound budget and a sensible roadmap for economic progress.

The Fiscal 1984 budget of $848.5 billion is based on four principles for deficit reduction. First, a comprehensive Federal spending freeze which will allow 1984 outlays to grow at the predicted rate of inflation. Second, a restructuring of programs in health care, federal retirement and welfare. Third, a reduction in defense spending of $55 billion over the next 5 years. And fourth, a standby deficit reduction program of tax increases to become effective in FY 1986 if the economy is not in recession, the proposed freezes have been enacted, and the deficit is greater than 2.5 percent of GNP.

All of these efforts are designed to reduce deficits from nearly 7 percent of GNP today to 2.4 percent by 1988, putting the budget on a path consistent with sustained economic recovery.

In the course of our deliberations over the past several weeks, it became clear that the recession had taken a high toll in revenues to the government. It became equally clear that decisive action had to be taken to reduce the share of GNP taken by the government, especially as the economy enters a period of growth.

I believe we have fashioned a reasonable approach to the deficit problem that should be credible to the financial markets, the Congress and the American people. We are renewing our commitment to limiting the tax burden, to reducing the growth of Federal spending, to eliminating excessive regulations, and to a moderate and steady monetary policy. At the same time, we have significant new initiatives to fight the most pressing problem in America today: unemployment.

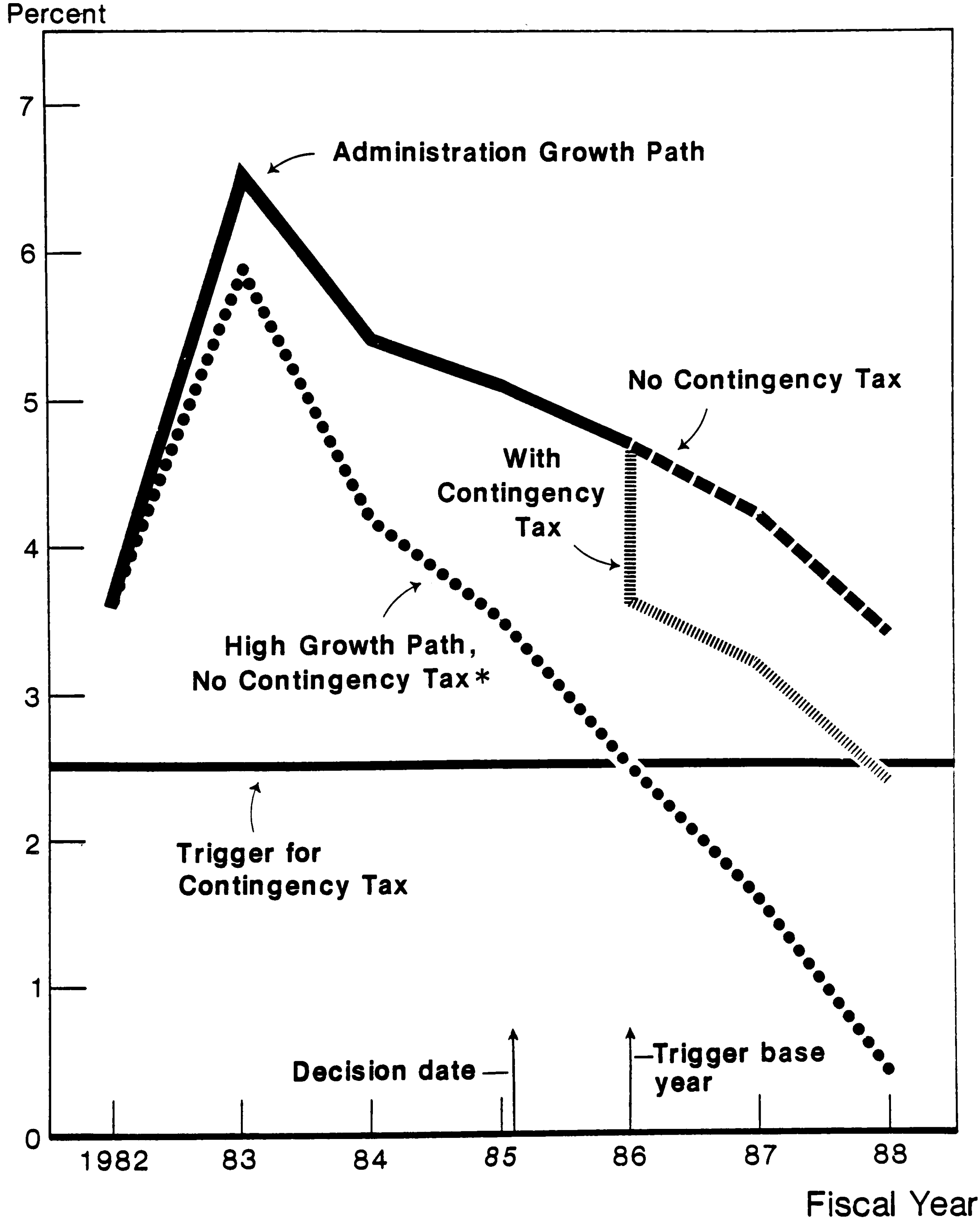
With that brief background, Marty will discuss the economic forecasts, Dave will outline the budget itself, and I will summarize the tax provisions. After those three presentations, we will take questions.

THE DEFICIT AS A SHARE OF GNP

The attached chart shows the downward path of federal deficits under the proposed budget. The heavy black line shows the rate of diminishing deficits under the Administration's projected rate of economic growth. With the contingency tax, and assuming all of the budget proposals are enacted by Congress, the deficit would fall steadily to just under 2-1/2 percent of GNP by 1988.

Assuming economic growth 1-1/3 percentage points faster than the official forecast, as shown by the heavy broken line, deficits would be under 2-1/2 percent of GNP by 1986 and there would be no need for the contingency tax.

THE DEFICIT AS A SHARE OF GNP



*Higher growth than the official path by 1-1/3 percentage point starting fiscal year 1983.

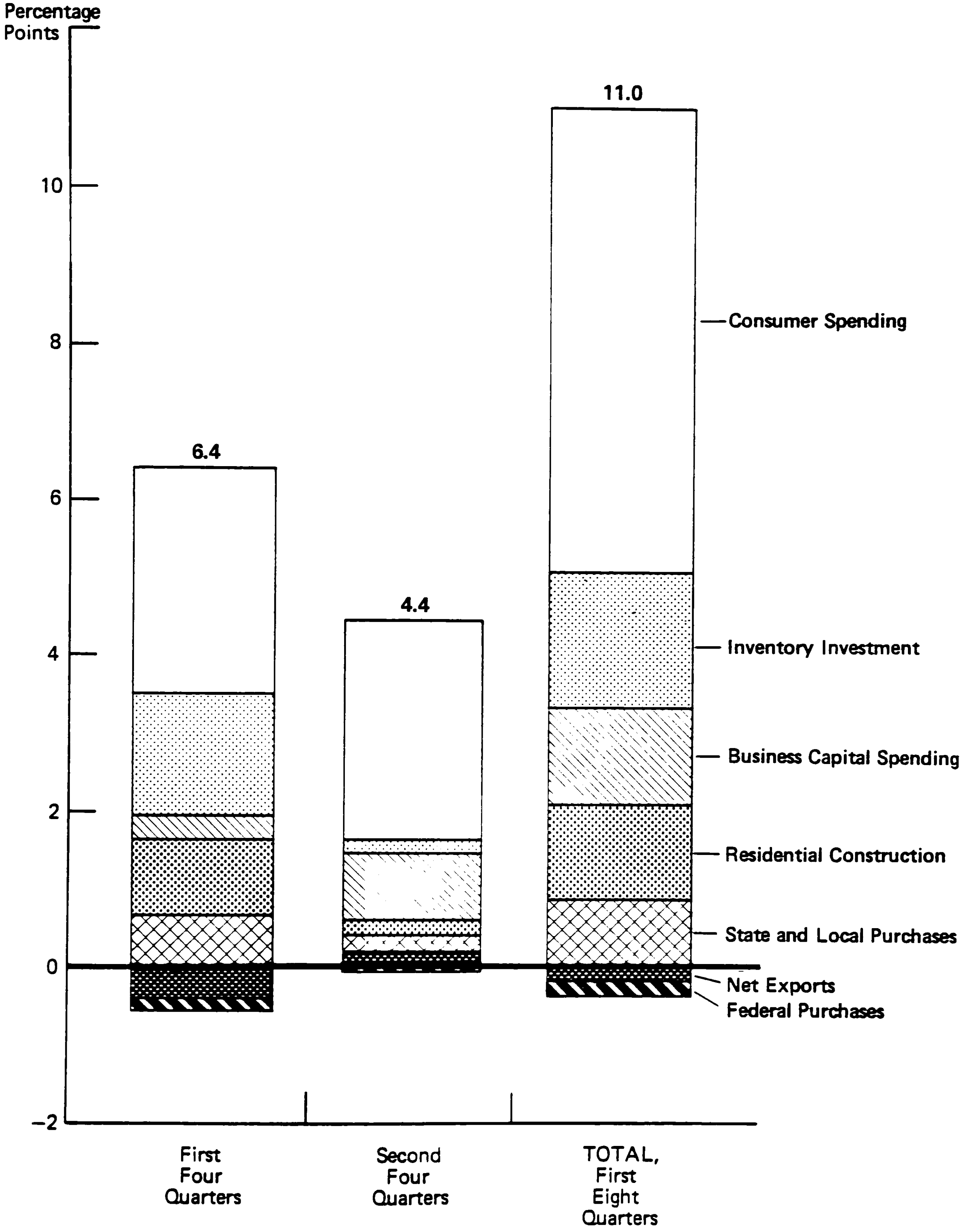
January 28, 1983-A214

THE TYPICAL RECOVERY

The attached chart shows that in the typical postwar recovery, total gains in GNP over the first eight quarters have come primarily from private sector spending. Very little comes from government spending. Although the present recovery may not be typical in magnitude, the relative size of the components will be the same.

As the chart indicates, most of the initial thrust of recovery comes from consumer spending, inventory investment, business capital spending, and homebuilding.

CONTRIBUTIONS TO A TYPICAL RECOVERY*
BY REAL GNP COMPONENT



* Average of postwar recoveries, excluding the Korean War period and the short-lived 1980-81 recovery.

January 21, 1983-A213

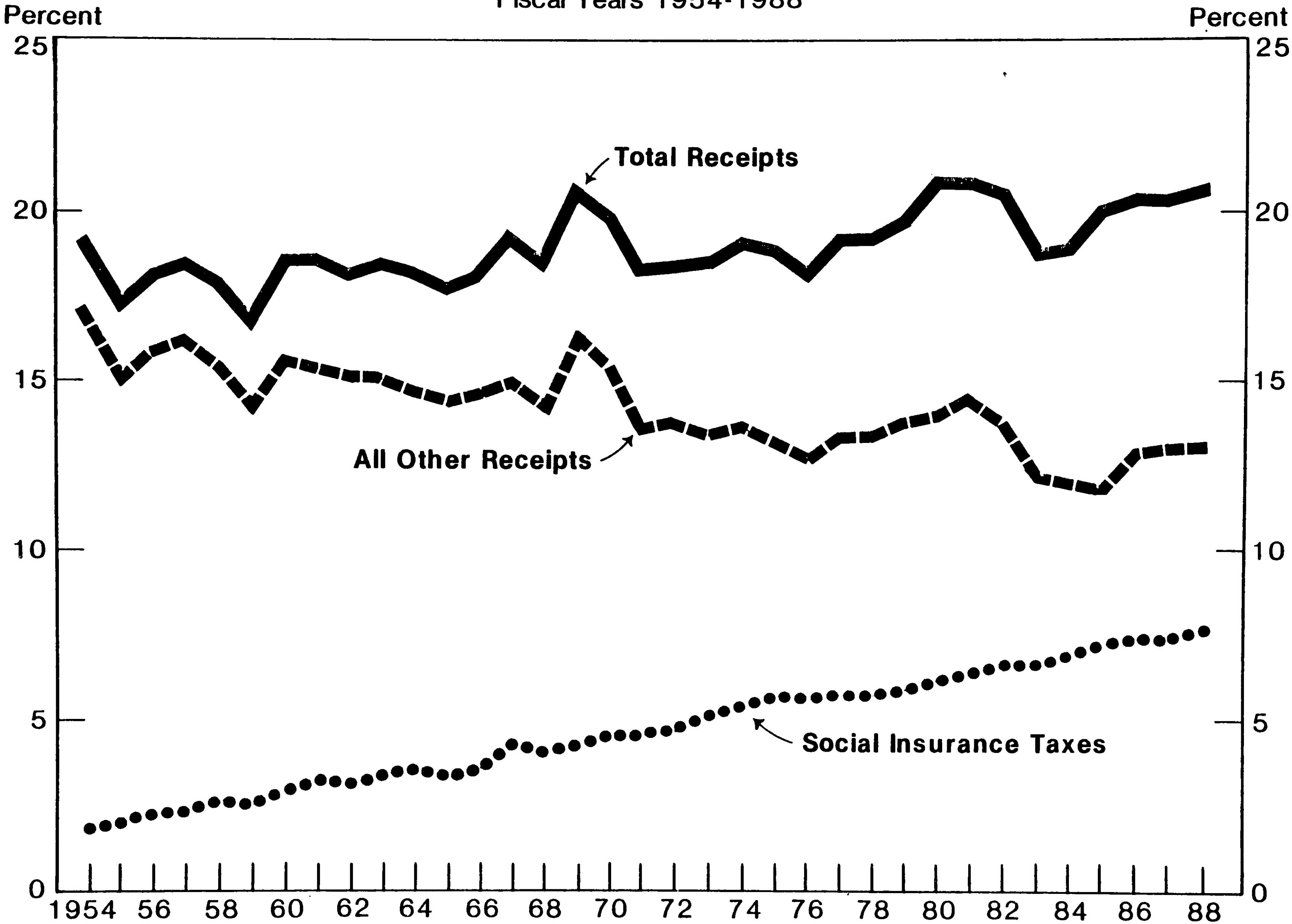
TAX REVENUES AS A PERCENT OF GNP

The attached chart shows that total tax revenues to the Government, as represented by the solid line, have increased slightly as a percent of GNP over the past 30 years. Revenues continue to increase in spite of the 25 percent tax cut enacted in 1981.

The heavy broken line (all other receipts) shows the level of tax revenues if social insurance taxes are excluded. As the dotted line shows, rising payroll taxes to support social security and other retirement obligations are the primary reason for the upward drift in the total tax burden over the past three decades.

UNIFIED BUDGET RECEIPTS AS A PERCENT OF GNP *

Fiscal Years 1954-1988



* Receipts include contingency taxes.

January 28, 1983-A215

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE UPON DELIVERY
EXPECTED AT 9:30 A.M.
Wednesday, February 2, 1983

TESTIMONY OF THE HONORABLE DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
HOUSE BUDGET COMMITTEE

Mr. Chairman and Members of the Committee:

It is a pleasure to meet with you today and to discuss the Administration's 1984 budget proposals. The development of a sound fiscal policy was one of the central objectives of the Reagan Administration when it came into office two years ago. For too long a time Americans had watched the share of GNP accounted for by Federal spending and taxes move upward. As the government siphoned off resources from the private sector and the money supply expanded, economic activity stagnated and inflation soared.

In February 1980 the Administration put before Congress a four point plan to revitalize the economy. Our program included spending restraint, tax reductions, regulatory reform, and support of the Federal Reserve's efforts to attain gradual, steady reduction in the rate of monetary growth.

The transition to a noninflationary environment has been somewhat more difficult than anticipated. We have seen two years of serious economic recession as a result of the inflation/tax spiral.

However, the worst is now over. There has been clear progress on inflation, and consumer price growth has dropped dramatically from 12.4 percent in 1980 to 3.9 percent in 1982. Interest rates are down from peak levels of 21-1/2 percent on the prime in December 1980 to 11 percent currently, and the stock market last year made new highs. Indicators such as housing, inventories, and real income show the economy is poised for recovery. Alongside these favorable developments, there remains distressingly high unemployment.

The task now is to encourage the renewal of economic growth to reduce unemployment and provide productive job opportunities in the private sector. In so doing we must not repeat the errors of the past and return to an inflationary economy.

The current domestic situation is complicated by the existence of large Federal budget deficits and the threat of even larger ones in years to come. These budget deficits will have to be reduced, since their persistence would inevitably lead to very adverse consequences for the U.S. economy and its financial markets.

Many of the economic difficulties we face at home are also faced by countries abroad. The entire international economy is experiencing a severe slowdown, complicated by the special debt-servicing problems of a number of countries. My prepared statement today deals primarily with the U.S. domestic economy, but it is obvious that the domestic and international situations are closely linked. The clear need in both cases is to encourage expansion rather than undergo further contraction.

It is important to recognize that current difficulties are the culmination of a long period of deteriorating economic performance in this country. The U.S. economy was in deep trouble long before the current recession began. It follows that our policies must aim at lasting long-run solutions. There are no quick cures.

Inflation has led to a roughly parallel rise in key interest rates. As shown in Chart I on interest rates and inflation, the 3-month Treasury bill rate followed the rate of inflation very closely over most of the period from the early 1960's to present. Thus, inflation appears to have been a major factor in the increase in the bill rate during that time.

Rising rates of inflation after the mid-1960's did not lead to more rapid economic growth for any sustained period of time. Quite the contrary. Inflation and its inevitable consequence of higher interest rates finally choked off real growth altogether.

Approach of the Reagan Administration

The Administration's primary economic goal upon coming to office was a fundamental restructuring of the economy, including:

- bringing inflation under control;
- shifting the composition of activity away from government spending toward more productive endeavors in the private sector;
- providing an environment which would reward innovation, work effort, saving and investment, and in which free-market forces could operate effectively.

Over the past two years we have seen evidence that the Administration's program is working. The fundamental elements of recovery are now largely in place. Inflation has been brought under control. Interest rates are coming down, as shown in Chart II. Real wage growth is being restored. In addition, there have been other improvements -- notably in productivity growth and saving behavior -- which mark a shift away from the problems that contributed to sluggish economic performance in recent years.

Within this framework of very significant achievements, there remains the fact that the economy has been in recession and unemployment is high. The unemployment rate of 10.8 percent in December is, of course, a matter of great concern. The President has indicated in his State of the Union Message that he will be submitting special legislation to help deal with the problem.

The Current State of the Economy

The economy now stands poised for recovery. In fact, the recovery may well already be underway at this moment. It has been much longer in coming than we, or for that matter nearly all forecasters, had expected.

The delay occurred primarily because of the persistence of high interest rates and because of developments in the international sphere. On the international front, the economies of our leading trading partners continued to weaken. Weakness among all the industrialized nations was self-reinforcing. Furthermore, the financial difficulties of some of the newly industrializing nations had adverse impacts on economic activity here. These forces, combined with a general hesitancy on the part of the consumer, led to another round of inventory cutting in the second half of 1982 and delayed the expected turnaround of the economy.

Signals of an Economic Upturn

There are now clear signals that the economy is turning around and that the recession will soon be behind us. To summarize these signals:

- The index of leading indicators has risen for eight out of the last nine months.
- Housing is in the midst of a rapid recovery.
- Business trimmed inventories sharply in the final quarter of last year. Historically, a cleanout of inventories typically has been followed by a shift back to higher rates of production.
- Retail sales have begun to firm.
- Total industrial production stabilized in December and appears poised to turn upward.

The Typical Recovery

We would all hope for a vigorous recovery, not unlike those which occurred in the past. The typical postwar recovery path is shown in Chart III. Excluded from it are two atypical recoveries -- the first of which included the Korean War buildup and the second which got underway late in 1980 but was short-lived. The five recoveries contained in the average line in the chart were remarkably similar. Gains over the first eight quarters from the real GNP trough were within an extremely narrow range of 5 to 6 percent at an annual rate.

The contributions of GNP components to real growth during the typical recovery are shown in Chart IV. As it indicates, much of the initial thrust for expansion comes from:

- a resurgence in homebuilding activity, such as currently is underway;
- a swing in inventory investment from decumulation in the later stages of recession to accumulation; and
- a major contribution from consumer spending, with purchases of consumer durables registering particularly large increases.

By contrast, Federal spending normally declines as a share of GNP during recovery, and is not necessary for promoting expansion.

The Outlook for the Economy

A vigorous recovery of the type outlined would be most welcome. It would certainly help ease the Nation's budgetary problems. However, we recognize that the serious problems still confronting us may well hold growth during the next year or two below the typical recovery pattern.

- Our overall trade balance is likely to register further marked deterioration in the coming year.
- Real interest rates may persist at high levels, though remaining below those prevailing a year ago.
- The economy is in the process of undergoing marked structural change. Some of our industries may not quickly regain the vitality they experienced in the 1950's and 1960's. The shift of resources to emerging industries will take time.
- Most fundamentally, we are not yet fully out of the inflationary woods, and we cannot afford to direct monetary and fiscal policy toward excessively rapid economic expansion.

For these reasons, the Administration is forecasting fairly modest real growth at a 3.1 percent rate during the four quarters of 1983, rather than the typical recovery growth rate of about twice that much, though certainly we would welcome a stronger recovery. Growth is expected to pick up modestly to the 4 percent range in 1984 and the years beyond.

Policies for the Recovery

In setting policy for the remainder of the 1980's, we must recognize what we must <u>not</u> do. We no longer have the freedom of action to revert back to the overly stimulative monetary and fiscal policies pursued at times in the past, for these would surely lead to a resurgence of inflationary pressures and a new round of rising interest rates. Further, we must not reverse the fundamental tax restructuring put in place in 1981, for this was designed to provide the noninflationary incentives without which the private sector would continue to wither.

Policies for a Changing Economic Structure

For years private sector initiative and dynamic market forces have been stifled by unnecessary Federal regulation. It is important that we carry through with policies of reducing the regulatory burden on private industry. Noteworthy successes have been achieved in this area, particularly in the deregulation of the financial system. For the first time in the postwar period, small investors can count on being able to obtain market rates of return on their savings from banks and thrift institutions.

Further, we recognize that our economy and those of the other industrialized nations are undergoing a period of restructuring. This is an era of rapid technological change, and comparative advantage in the production of many goods and services is shifting from the already developed to the newly developing nations. Those nations which expend all their energies shoring up declining industries and resisting change will find themselves with industrial bases that are obsolete and with declining relative standards of living. Their more foresighted and innovative neighbors will be moving forward and capturing newly opening markets.

Government can ease the painful process of structural change within the economy. The President has announced a program that relies heavily on the market mechanism to deal with structural unemployment that stems from problems in both labor and product markets. This program will emphasize training, retraining and relocation, and job-search assistance for workers facing the lack or loss of jobs even after an economic recovery. Other proposals will be designed to reduce the barriers to youth employment.

Finally, in setting the proper course of policy for the 1980's, we must work closely with the other industrialized and newly industrializing nations of the world. Negotiations are nearing completion on measures to assure that the International Monetary Fund has adequate resources to help countrie experiencing difficulties implement sound policies of economic adjustment. The negotiations are focusing in on an increase in IMF quotas to a new level in the range of $93-100 billion, representing an increase of 40-50 percent, and an expansion of the existing General Arrangement to Borrow (GAB) to a level of about $19 billion (from $7 billion). The participation of the United States in an increase in IMF resources is an essential complement to domestic measures to achieve sustainable economi growth and represents a valuable investment in defense of the economic interests of the American farmer, laborer, businessma and consumer. The U.S. share of the increase in quotas and the GAB will be about $8 billion but will have no effect on net budget outlays or the budget deficit since simultaneous with any transfers to the IMF, the U.S. receives an offsetting increase in its international monetary reserve assets.

Legislation providing for the U.S. share of the increase in IMF resources will be submitted in the near future and I urge prompt approval by the Congress.

Monetary Policy

In addition to policies aimed at facilitating structural changes within the economy, we must maintain steady monetary and fiscal policies directed at reinvigorating economic activity. Steady, predictable money supply growth at a noninflationary pace has been, and continues to be, one of the major goals of the Administration's economic program. The Federal Reserve's efforts to achieve that goal have been complicated by a number of factors, such as far-reaching institutional changes in the banking and thrift industries. Nevertheless, the Fed has generally been successful, albeit in a somewhat erratic fashion.

Monetary policy faced a difficult and uncertain situation during much of the last year. Rapid institutional change in the form of new money market instruments blurred the boundaries between the various aggregates and made the achievement of any target rates of growth unusually difficult. There is also some indication that the recession may have led to an increased demand for liquidity and precautionary balances. In 1982, growth in monetary velocity -- the rate at which money is used -- turned negative for the first time in nearly three decades. Under the unusual economic and institutional circumstances of 1982, some temporary offset in the form of above-target rates of monetary growth was probably desirable.

The Federal Reserve's efforts to slow money growth have been accompanied by some volatile short-run swings. Growth in M1 was actually negative on a 13-week basis by mid-summer of last year, and then soared to the double-digit range by the end of the year. This recent acceleration has caused some observers to conclude that the fight against inflationary money growth has been abandoned. That is not true. Both the Administration and the Federal Reserve remain committed to the long-run goal of providing money growth at a noninflationary pace consistent with a steady and sustainable expansion of economic activity.

Fiscal Policy

The objectives of our fiscal policy upon coming to office two years ago were two-fold. First, we believed and still believe it was imperative to correct the disincentives to economic performance that had been built into the tax structure over the years. These disincentives arose in large measure, not by design, but through the interaction of a high rate of inflation with a progressive tax system and historical cost accounting of depreciable assets. Second, it was equally

imperative to reverse the seemingly inexorable growth of Federal spending, thereby freeing resources for use in the private sector. In moving to achieve these goals, we faced one major constraint, namely that our defense establishment had been allowed to deteriorate badly, so that our national survival mandated a stepped-up rate of defense spending.

The tax reforms that were put in place were designed primarily to restore an adequate rate of return for investment in plant and equipment and to put a halt to the steady ratchet-ting upward of marginal tax rates on labor and savings income. The investment incentives were necessary to bring long-depress rates of business capital investment and productivity growth back up to acceptable standards. For individuals, the tax cuts were needed to protect incentives and purchasing power, and to keep American labor competitive in world markets. For the average taxpayer, they will only result in an actual dolla tax cut in 1983, after allowance for the effects of bracket creep and higher social security taxes. And that 1983 cut and tax indexing will be needed to offset bracket creep and increa in social security taxes scheduled to take effect in the futur These measures will greatly improve the competitive standing of American capital and labor in the world as economic recover proceeds.

We were relatively successful in working with the Congres to achieve our goals of tax reform, but we were less successfu in the area of outlay control. A major portion of the savings we had proposed in our original budget did not receive favorab action. This, along with much weaker economic activity than expected, has left us facing the prospect of large deficits even as the economy recovers.

The proposals in the FY-1984 Budget are directed at the crucial task of restoring noninflationary economic growth. This requires the preservation of the investment and work incentives provided by the tax reforms of 1981 and a reduction in the high deficits and interest rates which lie ahead unless corrective action is taken to bring government outlays under control.

The tax reforms already enacted will enable us to make go progress in rebuilding and modernizing America's plant and equ ment as the recovery progresses. Incentives are in place to encourage saving and investment and to lower the cost of new machinery and structures. Taxes on American labor are coming down. These reforms will lead to a more productive, more competitive United States. The capital formation program will be financed by higher levels of personal saving, more generous capital consumption allowances, and higher retained earnings as profits recover from the current slump. These elements, pl state and local budget surpluses, form the Nation's savings po

Spending reduction will contribute to the recovery, and the recovery will contribute to deficit reduction. The deficit will fall as the economy advances, particularly if the recovery is a vigorous one. A strong recovery with 1-1/3 percent more real growth per year than in our forecast would bring the budget to near balance by 1988, provided we also curb the growth of Federal outlays.

However, if we fail to bring spending under control and if recovery is slow, we will face a deficit problem which is larger and longer-lasting than we can afford. In such case, the deficit could run in the range of 6 to 7 percent of GNP each year through 1988. Our tax reforms were designed to raise the private savings share, but still we would face the possibility of draining off a large part of the pool of savings, leaving less available for new capital formation. Interest rates could remain high, and the recovery could stall.

This Administration is determined that deficits of such magnitudes will not come to pass. We came to office with a program of boosting the rate of capital investment in order to place the economy on a faster growth track, and we will not allow ourselves to be diverted from that goal. We will take whatever measures are necessary to narrow the deficit to acceptable levels.

- Preferably, all of the necessary narrowing of the deficit would come from the outlay side. Total Federal spending represents the amount of resources absorbed by the government at the expense of the private sector. This spending can be financed by both taxes and borrowing, which in either case amounts to a drain on private resources. Only through spending reduction will the credit market find itself in a more favorable position.

- In the event that the combination of economic growth and outlay reductions is not sufficient to narrow the deficit to acceptable levels in the outyears, we are prepared to request additional revenue raising measures in those years. If the Congress chooses not to reduce spending, as we wish, then it is preferable to have the full cost of federal spending programs explicitly identified for the taxpayers who bear the burden of financing government. If additional revenues are needed, this Administration will do its best to structure the tax code in a way that minimizes disincentives for productive effort.

Our Budget Proposals

Spending reduction is crucial. Unfortunately, it has be difficult to achieve because of the built-in momentum of Fede spending programs. Consequently, we are proposing strong medicine. None of us will find it agreeable, but it is criti to the restoration of vitality to our economy. In prescribin the medicine, there must be assurance all will be willing to t the proper dosage, just as all of us will share in the benefi of a revitalized recovery. We, like a great many other natio in the world, have tried to live beyond our means. Now we mus bring our spending into line with our productive capacity and strengthen the private sector which produces our national weal

The deficit reduction program that we propose contains fo basic elements.

- The first is a freeze on 1984 outlays to the extent possible. Total outlays shall be frozen in real terms in 1984. The 6-month freeze on COLAs, as recommended by the Social Security Commission, is to be extended to other indexed programs. There will b a 1-year freeze on pay and retirement of Federal workers, both civilian and military. Many workers in the private sector have accepted freezes in thei pay. Federal workers can also make a sacrifice, which hopefully will serve as an example for sector of the economy which have not yet recognized the need for moderation in wage demands. As a final ite of freeze, outlays for a broad range of nonentitleme programs will be held at 1983 levels.

- The second element of our budgetary program contain measures to control the so-called "uncontrollables." Laws have been so written that Federal payments are automatic to all those declared eligible. We plan a careful review of all such programs, taking special care to protect those truly in need.

- The third element is a cutback of $55 billion in defense outlays from original plans.

- Fourth is a set of proposals involving the revenue side of the budget, described below.

We are projecting receipts for the current year (fiscal year 1983) of $597.5 billion. For fiscal year 1984 we expect receipts to be $659.7 billion. The 1983 figure represents a decline of $20.3 billion from the fiscal year 1982 total of $617.8 billion. This decline, and indeed the absence of an increase in receipts in the range of $50-70 billion, is explained primarily by the recession. As I have already explained, our economic projections throughout the remainder of the recovery period are cautious. If real GNP grows at a faster rate than we have projected, then receipts for the current fiscal year, as well as for subsequent years, will be somewhat higher than we are now projecting.

In 1984, as the recovery is well underway, receipts are expected to rise to $659.7 billion, an increase over 1983 of $62.2 billion, representing an annual growth of 10.4 percent. This will occur as profit margins recover and other income shares continue to grow.

For the other years in our forecast period (1985-1988) we project an average annual growth rate of receipts about 10 percent without contingency taxes (and 11 percent per year including contingency taxes), with receipts reaching the $1 trillion mark for the first time in fiscal year 1988. All of these projections assume the legislative proposals included in the President's Fiscal Year 1984 Budget. Receipts under existing legislation will also grow, but at a somewhat lower 9-1/2 percent annual average rate.

It is noteworthy that individual income tax receipts will continue to rise over the 1985-1988 period, but only as <u>real</u> income rises. Beginning in 1985, we will no longer collect hidden taxes in the form of bracket creep caused by inflation. Without the indexation provision of ERTA, individuals would pay $6 billion more in taxes during fiscal year 1985 alone, and about $100 billion more during the entire forecast period -- 1985 through 1988.

There has been a gradual upward trend in unified budget receipts as a percent of GNP, shown in the top line of Chart V. As shown in the bottom line of the chart, a major shift in the composition of receipts has been the rising share of social insurance and other payroll taxes to fund social security and other retirement benefits.

There is no proposed omnibus tax bill in the President's budget message. However, there are several separate tax items. Proposed tax legislation in the President's budget can be conveniently grouped under three broad headings: Proposals that improve the income security of Americans, proposals that will improve our ability to produce future output, and, as an insurance policy, a contingency or standby tax, which is intended as a clear signal that we will not permit spending to increase in the outyears unless we pay for it up front.

In the first category, our principal recommendation is for adoption of the bipartisan social security proposals. These proposals, which will increase receipts to the social security funds by $9.8 billion in fiscal year 1984, $11.6 billion in 1985, and $10.6 billion in 1986, are necessary to insure the solvency and security of these trust funds.

The second category, proposals to improve the utilizatior of our human resources, includes the tuition tax credit, the exclusion of earnings on savings for higher education, the jot tax credit for hiring the long-term unemployed, and the enterprise zone tax incentives. These will all improve our product capacity, either through increased investments in education oı more directly, by getting our currently underutilized force of experienced workers back to work. As a group, these proposals will reduce taxes $0.5 billion in 1984, $1.2 billion in 1985, and $1.7 billion in 1986.

Finally, the President has proposed a contingency tax pla designed to raise revenues of about 1 percent of GNP in the event that, after Congress has adopted the spending reduction proposals, there is insufficient economic growth to reduce the deficit below 2-1/2 percent of GNP. The contingency tax plan would not go into effect on October 1, 1985, unless the econom is growing on July 1, 1985. The contingency tax plan is an insurance program. It is important to have a plan in place so that the country and the world know that we will not tolerate a string of deficits that would exceed 2-1/2 percent of GNP. Chart VI shows the effect on the deficit that the contingency tax would have if it were implemented. It also shows how the budget picture would be altered by the stronger expansion that some private forecasters expect. The deficit path under high growth reflects the assumption that real GNP increases 1-1/3 percentage points faster than in the official forecast path, starting with FY-1983. Such growth would be in line with the performance from the end of 1960 to late 1966.

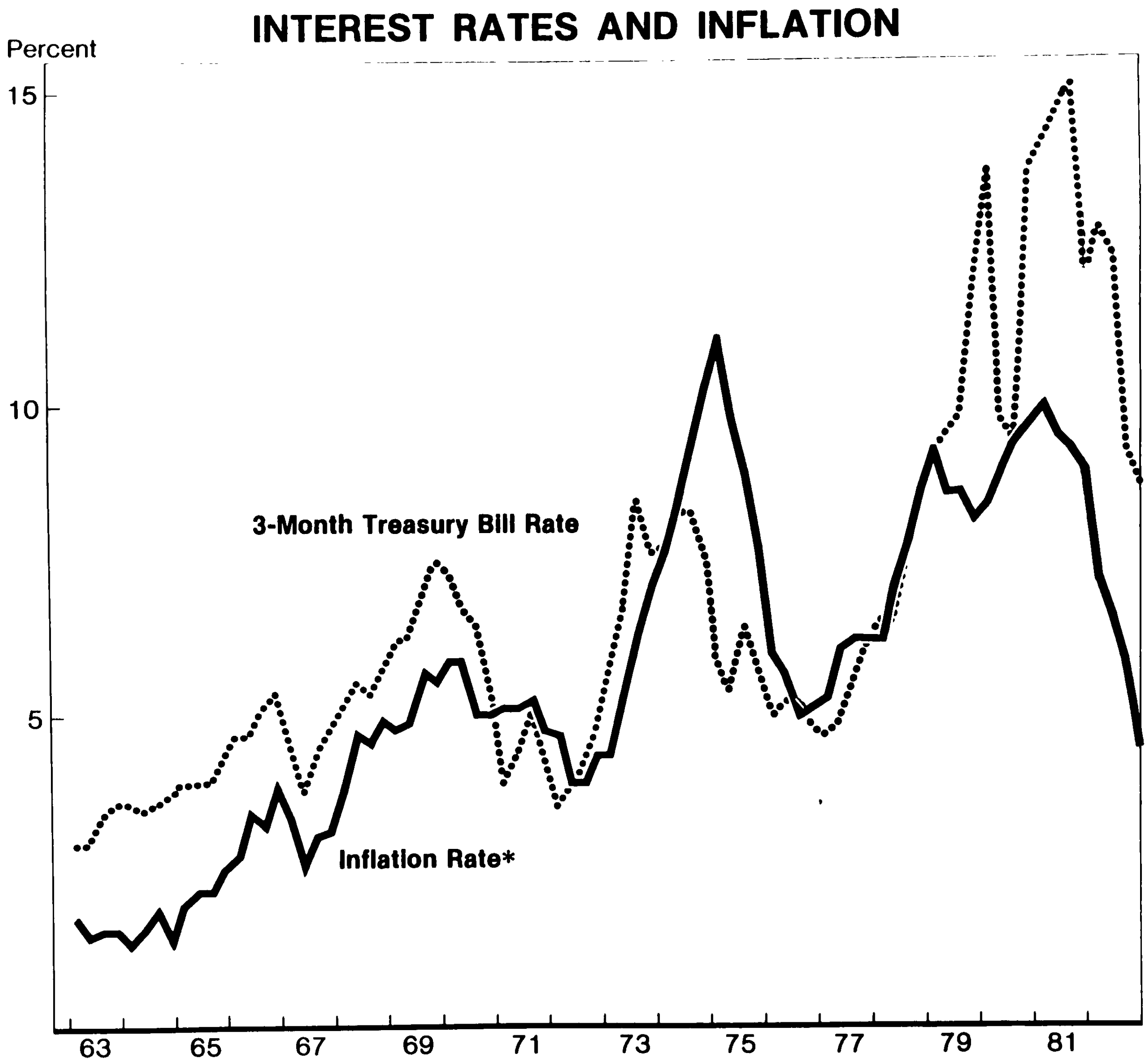
The contingency tax plan would contain two elements, each raising about half of the revenues that may be required. One element would be a temporary surcharge of 5 percent on individ and corporations. The other element would be a temporary excise tax on domestically produced and imported oil designed to raise revenues of about $5 per barrel. The contingency tax alternative shown in the budget raises $146 billion over the 36-month period beginning October 1, 1985. The specific contingency tax plan we will be sending to Congress for adoption this year will be designed to raise revenues of about $130-15(billion over a temporary period of up to 36 months.

If these budget saving proposals are enacted, we will reduce the projected deficits by a total of $580 billion over the next five years, or by $2,400 for every man, woman, and child in the United States. The deficit as a share of GNP will be down to about 2-1/2 percent in 1988 from the 6-1/2 percent we expect this year. Total outlays will grow by only 7 percent per year in nominal terms over the next five years, compared with a bloated 13 percent between 1977 and 1981.

In addition, as part of our overall program, over the next year we will be taking a careful look at the entire structure of our tax system. We will be searching for ways to simplify the tax code and make it fairer while at the same time promoting economic growth by enhancing incentives for work effort, saving, and investment. This is the true road for putting people back to work and bringing the budget into balance.

We are confident that the deficit reduction program contained in this realistic budget is the right program for the economy at this critical juncture. The most important signals we can send the economy are spending restraint, deficit restraint, and a commitment to non-inflationary economic growth throughout the decade. This is the program we have devised. Together with the Congress, we can make it work.

Chart I



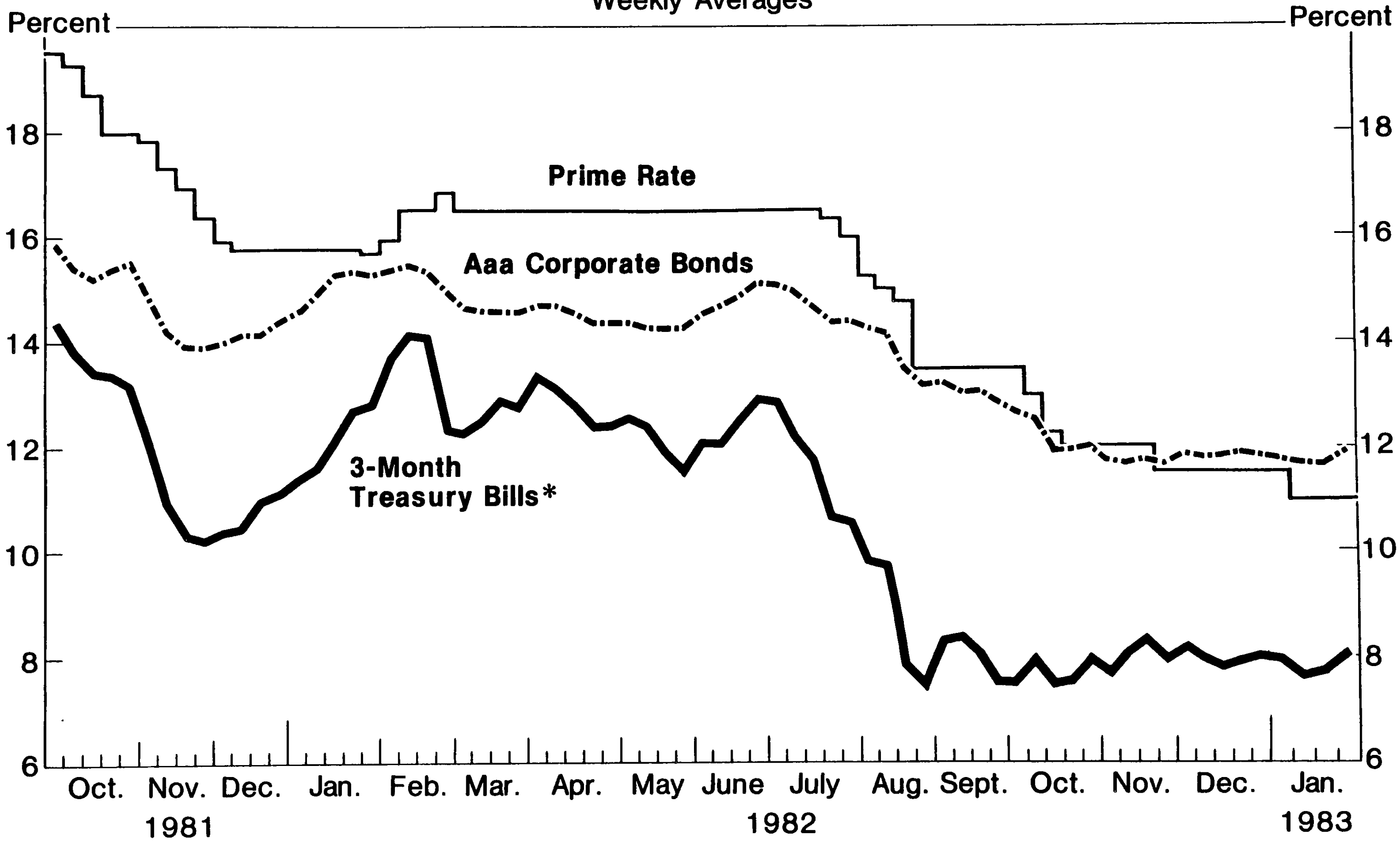
* Growth from year earlier in GNP deflator.
Plotted quarterly.

January 19, 1983-A28

Chart II

INTEREST RATES

Weekly Averages

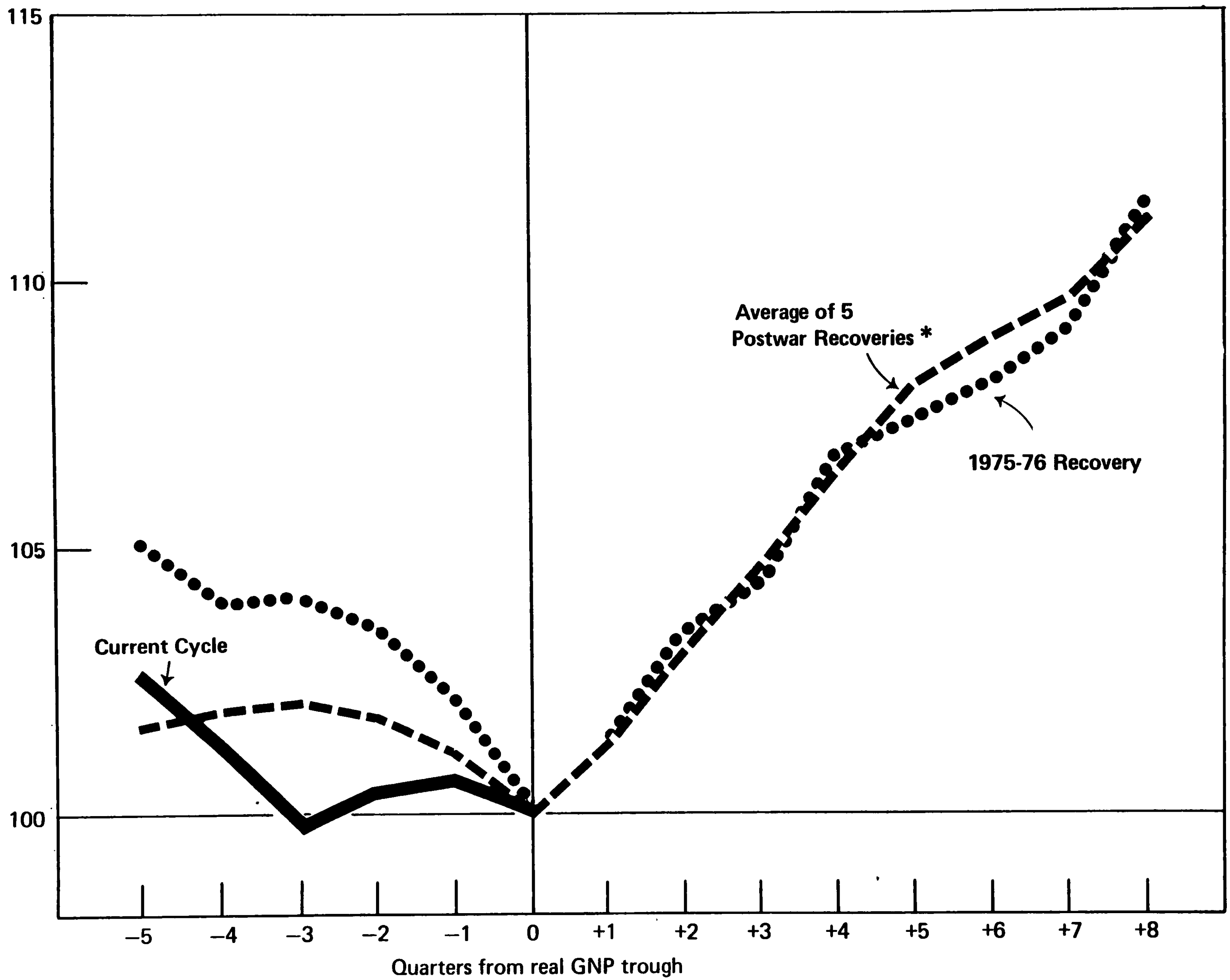


*Bank discount basis

January 31, 1983-A203

THE PATH OF POSTWAR ECONOMIC RECOVERIES

Real GNP trough = 100

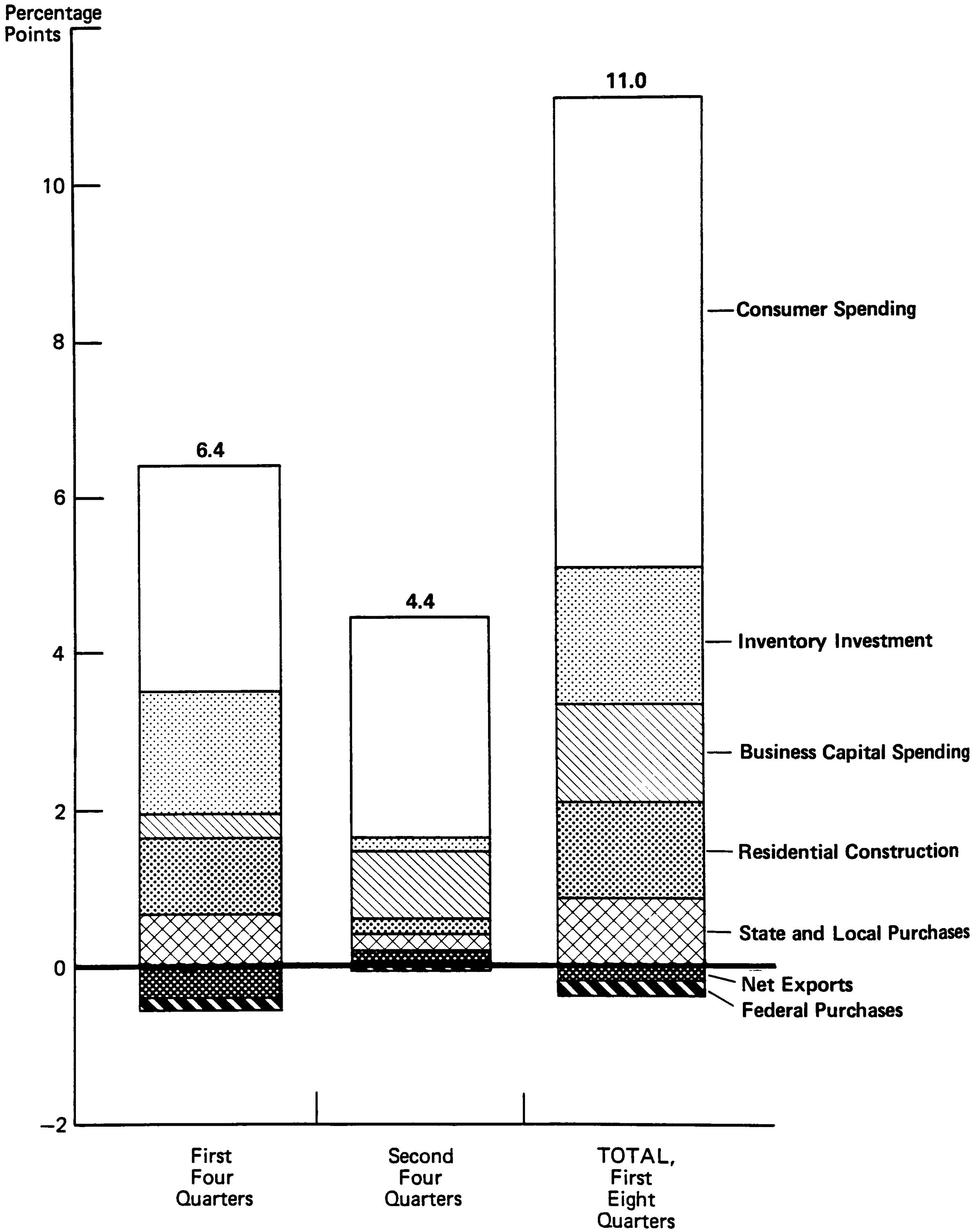


* Postwar recoveries excluding the Korean War period and the short-lived 1980-81 recovery.

January 25, 1983-A210

Chart IV

CONTRIBUTIONS TO A TYPICAL RECOVERY*
BY REAL GNP COMPONENT

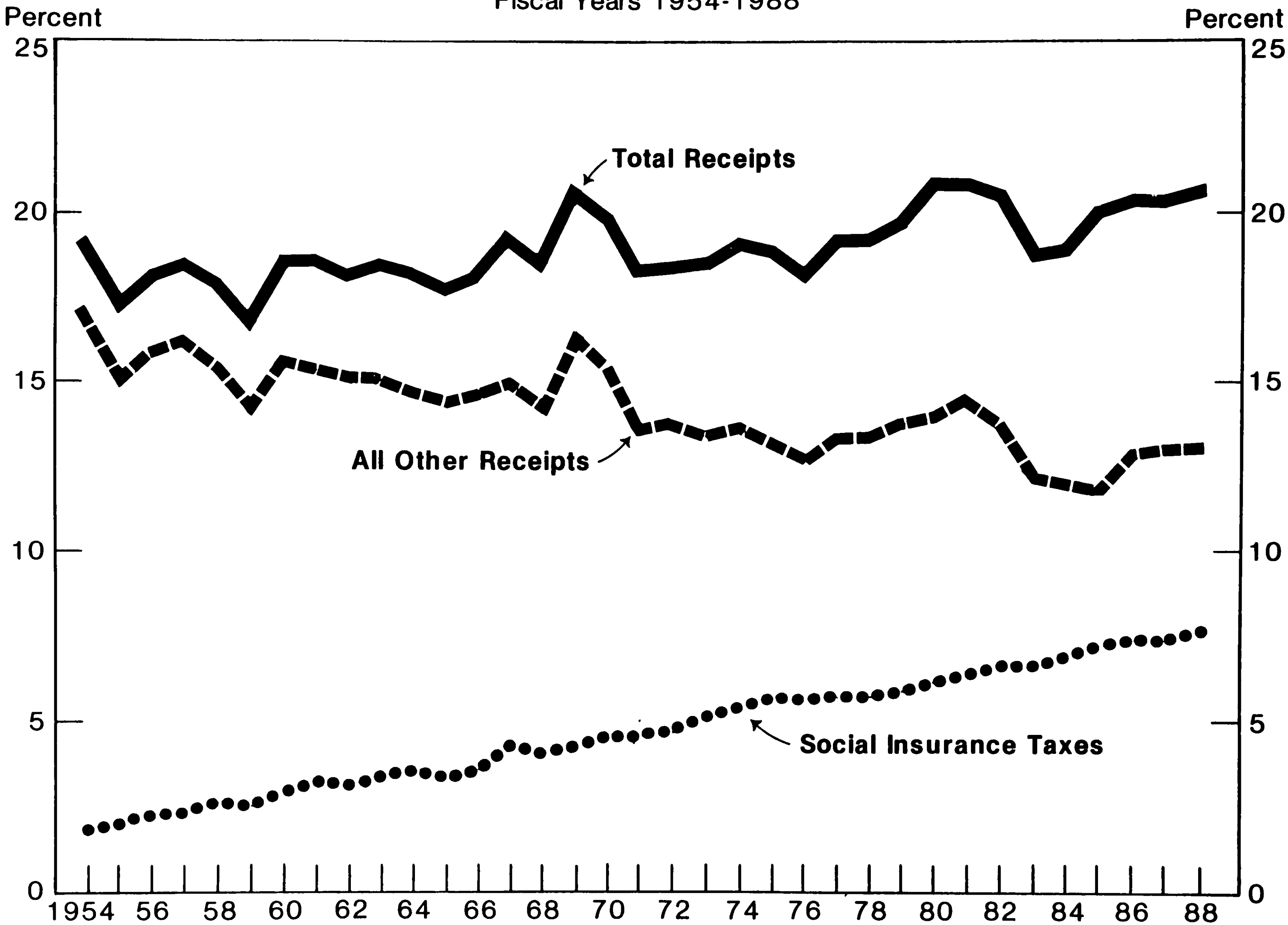


* Average of postwar recoveries, excluding the Korean War period and the short-lived 1980-81 recovery.

January 21, 1983-A

UNIFIED BUDGET RECEIPTS AS A PERCENT OF GNP *

Fiscal Years 1954-1988

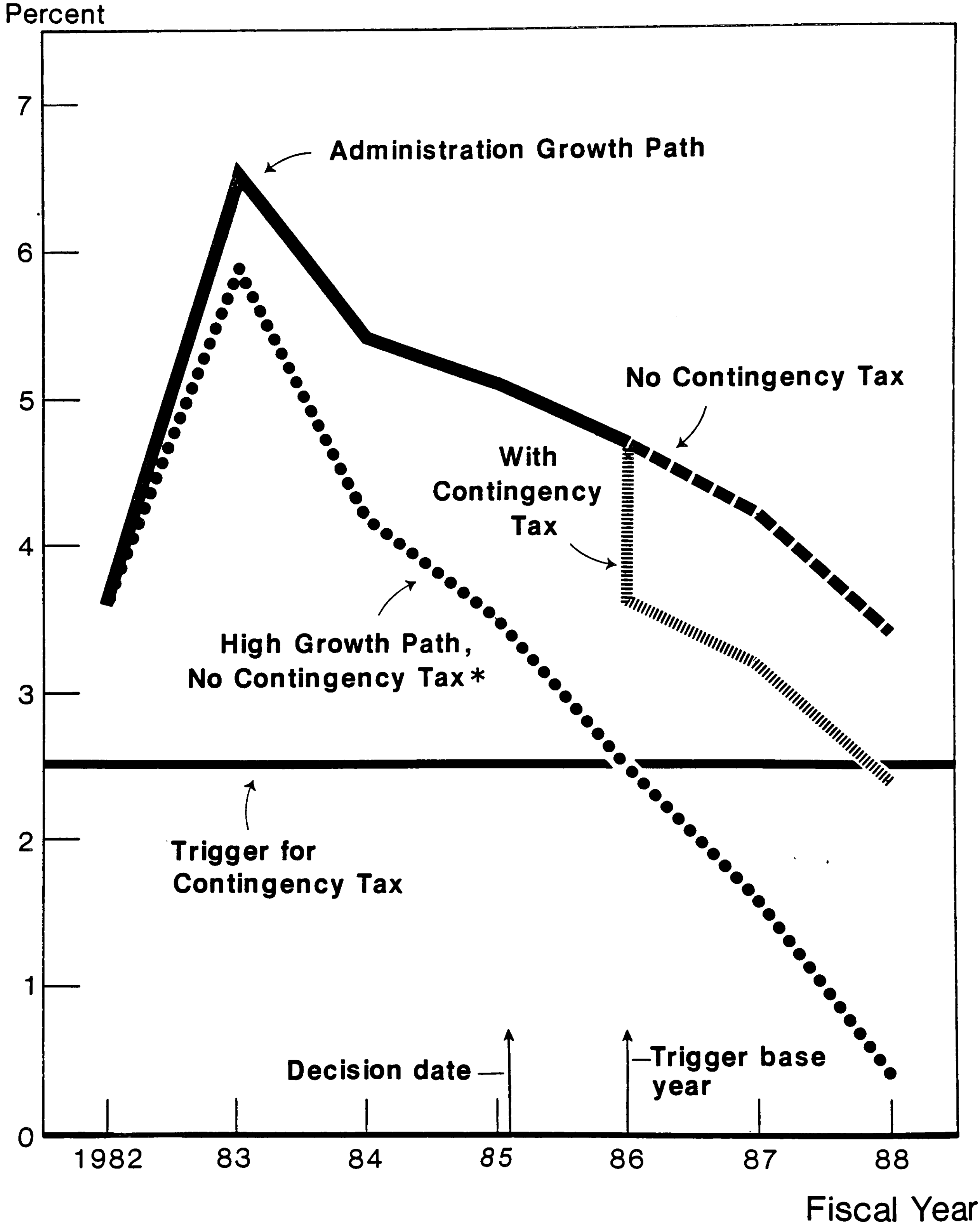


* Receipts include contingency taxes.

January 28, 1983-A215

Chart VI

THE DEFICIT AS A SHARE OF GNP



*Higher growth than the official path by 1-1/3 percentage point starting fiscal year 1983.

January 28, 1983-A214

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE February 1, 1983

RESULTS OF AUCTION OF 3-YEAR NOTES

The Department of the Treasury has accepted $6,501 million of $12,292 million of tenders received from the public for the 3-year notes, Series L-1986, auctioned today. The notes will be issued February 15, 1983, and mature February 15, 1986.

The interest rate on the notes will be 9-7/8%. The range of accepted competitive bids, and the corresponding prices at the 9-7/8% interest rate are as follows:

	Bids	Prices
Lowest yield	9.90%	99.936
Highest yield	10.02%	99.632
Average yield	9.98%	99.733

Tenders at the high yield were allotted 6%.

TENDERS RECEIVED AND ACCEPTED (In Thousands)

	Received	Accepted
Boston	$ 69,520	$ 54,240
New York	9,661,295	5,209,755
Philadelphia	23,610	19,670
Cleveland	146,920	127,190
Richmond	127,580	94,120
Atlanta	83,795	80,930
Chicago	1,156,145	298,140
St. Louis	200,805	137,515
Minneapolis	84,060	84,060
Kansas City	122,175	120,205
Dallas	63,650	47,950
San Francisco	549,875	224,015
Treasury	2,770	2,770
Totals	$12,292,200	$6,500,560

The $6,501 million of accepted tenders includes $1,535 million of noncompetitive tenders and $4,966 million of competitive tenders from the public.

In addition to the $6,501 million of tenders accepted in the auction process, $420 million of tenders was awarded at the average price to Federal Reserve Banks as agents for foreign and international monetary authorities. An additional $1,100 million of tenders was also accepted at the average price from Government accounts and Federal Reserve Banks for their own account in exchange for maturing securities.

R-2013

federal financing bank NEWS
WASHINGTON, D.C. 20220
Press inquiries: 202-566-2615

FOR IMMEDIATE RELEASE February 2, 1983

FEDERAL FINANCING BANK ACTIVITY

Francis X. Cavanaugh, Secretary, Federal Financing Bank (FFB), announced the following activity for the month of October 1982.

FFB holdings of obligations issued, sold, or guaranteed by other Federal agencies on October 31, 1982 totaled $125.1 billion, an increase of $0.7 billion over the September 30 level. FFB increased holdings of agency debt issues by $0.2 billion and holdings of agency guaranteed debt by $0.6 billion. Holdings of agency assets purchased decreased by $0.1 billion. A total of 259 disbursements were made during the month.

Attached to this release are tables presenting FFB loan activity and new FFB commitments to lend during October and a table summarizing FFB holdings as of October 31, 1982.

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R-2014

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
ON-BUDGET AGENCY DEBT					
TENNESSEE VALLEY AUTHORITY					
Note #264	10/8	$ 5,000,000.00	1/7/83	8.097%	
Note #265	10/15	15,000,000.00	1/6/83	7.823%	
Note #266	10/22	5,000,000.00	1/6/83	7.897%	
Note #267	10/31	150,000,000.00	1/6/83	8.254%	
NATIONAL CREDIT UNION ADMINISTRATION					
Central Liquidity Facility					
Note #116	10/4	2,500,000.00	11/3/82	7.680%	
Note #117	10/12	1,569,340.00	1/10/83	8.099%	
Note #118	10/13	240,000.00	1/11/83	7.802%	
Note #119	10/14	12,000,000.00	1/12/83	7.771%	
Note #120	10/15	2,000,000.00	11/15/82	7.885%	
°Note #121	10/15	11,600,000.00	11/15/82	7.885%	
°Note #122	10/15	15,000,000.00	12/14/82	7.885%	
Note #123	10/18	14,450,000.00	11/29/82	7.901%	
Note #124	10/19	5,000,000.00	11/18/82	7.810%	
Note #125	10/25	1,500,000.00	12/30/82	7.985%	
Note #126	10/26	731,200.00	1/24/83	8.436%	
Note #127	10/26	3,000,000.00	12/30/82	8.436%	
Note #128	10/29	324,000.00	1/27/83	8.275%	
GOVERNMENT - GUARANTEED LOANS					
DEPARTMENT OF DEFENSE - FOREIGN MILITARY SALES					
Greece 14	10/1	3,485,769.00	4/30/11	11.826%	
Jordan 8	10/1	2,511,321.00	3/16/90	11.740%	
Sudan 4	10/1	19,982,203.73	2/10/12	11.828%	
Turkey 9	10/1	403,316.06	6/22/92	11.818%	
Uruguay 2	10/1	169,800.00	12/31/84	11.867%	
Israel 8	10/5	1,500,000.00	9/1/09	11.834%	
Israel 8	10/6	1,908,025.62	9/1/09	11.806%	
Israel 13	10/6	7,828,051.39	2/16/12	11.820%	
Turkey 11	10/6	1,244,493.00	12/22/10	11.813%	
Dominican Republic 5	10/7	79,749.52	4/30/89	11.528%	
Honduras 8	10/7	626,764.00	4/25/94	11.627%	
Greece 15	10/7	4,546,799.00	6/15/12	11.674%	
Turkey 9	10/7	6,486,945.05	6/22/92	11.624%	
Israel 8	10/12	70,000,000.00	9/1/09	11.084%	
Israel 13	10/12	808,239.28	2/16/12	11.128%	
Egypt 3	10/13	1,970,684.54	6/15/12	10.778%	
El Salvador 4	10/13	109,321.00	12/5/93	10.614%	
Indonesia 7	10/13	214,802.76	3/20/90	10.378%	
Philippines 7	10/13	343,597.38	9/10/87	10.133%	
Tunisia 10	10/13	714,313.75	10/1/93	10.558%	
Tunisia 11	10/14	23,968,728.25	5/5/92	10.444%	
Turkey 9	10/14	419,895.23	6/22/92	10.451%	
Turkey 9	10/15	6,486,960.11	6/22/92	10.669%	
Turkey 11	10/15	1,003,022.09	12/22/10	10.808%	
Israel 13	10/18	11,424,700.00	2/16/12	10.982%	
Egypt 3	10/19	704,544.32	6/15/12	10.850%	
Israel 8	10/19	25,784,000.00	9/1/09	10.806%	
Jordan 7	10/19	415,370.00	3/16/90	10.422%	
Somalia 1	10/19	1,776,675.60	9/1/92	10.618%	
Israel 13	10/20	6,050,640.70	2/16/12	10.820%	
Egypt 3	10/22	1,987,388.22	6/15/12	10.925%	
Honduras 5	10/22	225,000.00	4/25/90	10.537%	
Greece 14	10/22	263,750.00	4/30/11	10.915%	
Honduras 8	10/22	293,151.64	4/25/94	10.781%	
Israel 8	10/22	1,000,000.00	9/1/09	10.898%	
Panama 4	10/22	193,813.20	5/25/89	10.563%	
Peru 7	10/22	83,911.93	2/15/88	10.372%	
Somalia 1	10/22	654,631.64	9/1/92	10.725%	
Spain 4	10/22	841,774.12	4/25/90	10.536%	
Spain 5	10/22	2,364,331.75	6/15/91	10.596%	
[illegible]	[illegible]/26	7,549,264.88	2/16/12	11.286%	

OCTOBER 1982 ACTIVITY

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual	INTEREST RATE (other than semi-annual)
DEPARTMENT OF DEFENSE - FOREIGN MILITARY SALES (Cont'd)					
Lebanon 4	10/26	$ 81,739.00	7/25/89	10.994%	
Ecuador 4	10/28	317,017.31	7/25/87	10.502%	
Lebanon 4	10/28	4,211,953.00	7/25/89	10.786%	
Thailand 7	10/28	105,066.50	8/25/86	10.345%	
Egypt 3	10/29	10,949,689.54	6/15/12	11.048%	
Jordan 7	10/29	1,203,231.00	3/16/90	10.617%	
Liberia 9	10/29	860,907.15	7/21/94	10.862%	
Philippines 7	10/29	267,297.03	9/10/87	10.400%	
Spain 5	10/29	613,661.00	6/15/91	10.679%	
Turkey 13	10/29	1,215,659.00	3/24/12	11.043%	
DEPARTMENT OF ENERGY					
Geothermal Loan Guarantees					
Nothern California Municipal Power Corp. #2	10/1	4,281,088.88	10/1/83	10.385%	10.254% qtr.
Synthetic Fuels Guarantees - Non-Nuclear Act					
Great Plains Gasification Assoc. #32	10/4	4,000,000.00	7/1/02	12.581%	
#33	10/12	23,500,000.00	7/1/02	11.817%	
#34	10/18	5,000,000.00	1/3/83	8.635%	
#35	10/25	6,000,000.00	7/1/02	11.594%	
DEPARTMENT OF HOUSING & URBAN DEVELOPMENT					
Community Development Block Grant Guarantees					
Hammond, IN	10/4	339,168.00	5/1/84	10.885%	11.181% ann.
Ashland, KY	10/8	158,200.00	2/15/83	8.645%	
Syracuse Ind. Dev. Auth., NY	10/8	56,000.00	7/1/03	11.091%	11.399% ann.
Lawrence, MA	10/13	80,000.00	1/1/83	7.802%	
Owensboro, KY	10/13	201,187.53	9/1/83	8.715%	8.880% ann.
Tempe, AZ	10/13	119,000.00	6/1/83	8.465%	8.561% ann.
Washington County, PA	10/13	158,251.39	8/1/83	8.625%	8.811% ann.
Pittsburgh, PA	10/15	253,500.00	10/15/02	10.724%	11.012% ann.
Long Beach, CA	10/18	100,000.00	2/1/85	9.863%	10.106% ann.
Rochester, NY	10/22	160,000.00	8/31/03	10.865%	11.160% ann.
Kenosha, WI	10/28	63,515.00	6/1/83	9.085%	9.150% ann.
Washington County, PA	10/28	42,264.00	8/1/83	9.225%	9.371% ann.
Louisville, KY	10/29	300,000.00	11/30/82	8.275%	
Public Housing Notes					
Sale #26	10/8	34,758,641.96	11/1/91-- 11/1/18	11.745%	12.090% ann.
NATIONAL AERONAUTICS AND SPACE ADMINISTRATION					
Space Communications Company	10/1	9,100,000.00	10/1/92	11.804%	12.152% ann.
	10/20	7,500,000.00	10/1/92	10.562%	10.841% ann.
RURAL ELECTRIFICATION ADMINISTRATION					
*N. Michigan Electric #101	10/1	2,331,000.00	10/1/84	11.355%	11.198% qtr.
Arkansas Electric #142	10/1	1,722,000.00	10/1/84	11.355%	11.198% qtr.
Arkansas Electric #221	10/1	11,508,000.00	10/1/84	11.355%	11.198% qtr.
Western Illinois Power #225	10/1	10,706,000.00	12/31/16	11.882%	11.711% qtr.
°United Power #2	10/1	9,000,000.00	12/31/11	11.843%	11.673% qtr.
*Arkansas Electric #97	10/1	42,000.00	10/1/84	11.355%	11.198% qtr
*Arkansas Electric #142	10/1	3,980,000.00	10/1/84	11.355%	11.198% qtr.
*Hoosier Energy #107	10/2	25,000,000.00	12/31/13	11.701%	11.535% qtr.
*Alabama Electric #26	10/2	11,000,000.00	12/31/12	11.688%	11.522% qtr.
*Big Rivers Electric #58	10/2	1,369,000.00	10/2/85	11.505%	11.344% qtr.
*Big Rivers Electric #91	10/2	355,000.00	10/2/85	11.505%	11.344% qtr.
*Dairyland Power #54	10/3	2,000,000.00	10/3/84	11.255%	11.101% qtr.
°United Power #2	10/5	12,000,000.00	12/31/11	11.877%	11.706% qtr.

*maturity extension
°early extension

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
RURAL ELECTRIFICATION ADMINISTRATION (Cont'd)					
°United Power #6	10/5	$ 1,700,000.00	12/31/11	11.877%	11.706% qtr.
°New Hampshire Electric #192	10/5	100,000.00	12/31/15	11.912%	11.740% qtr.
°New Hampshire Electric #192	10/5	3,000,000.00	12/31/15	11.912%	11.740% qtr.
°New Hampshire Electric #192	10/5	2,460,000.00	12/31/15	11.912%	11.740% qtr.
°New Hampshire Electric #192	10/5	51,000.00	12/31/15	11.912%	11.740% qtr.
*Western Illinois Power #162	10/6	4,245,000.00	12/31/14	11.882%	11.711% qtr.
*East Ascension Tele. #39	10/6	622,000.00	12/31/12	11.864%	11.693% qtr.
Wolverine Electric #233	10/7	18,236,000.00	10/7/84	11.335%	11.179% qtr.
°New Hampshire Electric #192	10/7	3,242,000.00	12/31/16	11.770%	11.602% qtr.
Sunflower Electric #174	10/7	2,000,000.00	10/7/84	11.335%	11.179% qtr.
*Cajun Electric #163	10/7	14,398,000.00	12/31/14	11.754%	11.586% qtr.
New Hampshire Electric #234	10/7	26,598,000.00	10/7/84	11.335%	11.179% qtr.
Wabash Valley Power #104	10/8	8,809,000.00	10/8/84	10.585%	10.449% qtr.
Wabash Valley Power #206	10/8	1,511,000.00	10/8/84	10.585%	10.449% qtr.
*Hoosier Energy #107	10/9	30,000,000.00	10/9/84	10.275%	10.146% qtr.
*N. Michigan Electric #101	10/10	1,968,000.00	10/10/85	10.665%	10.526% qtr.
*N. Michigan Electric #101	10/10	786,000.00	10/10/84	10.275%	10.146% qtr.
*Wolverine Electric #100	10/10	1,559,000.00	10/10/85	10.665%	10.526% qtr.
Wolverine Electric #233	10/12	3,864,000.00	10/12/84	10.275%	10.146% qtr.
Western Farmers Electric #64	10/12	536,000.00	12/31/16	11.256%	11.102% qtr.
Western Farmers Electric #133	10/12	4,000,000.00	12/31/16	11.256%	11.102% qtr.
Western Farmers Electric #196	10/12	73,000.00	12/31/16	11.256%	11.102% qtr.
Western Farmers Electric #220	10/12	5,000,000.00	12/31/16	11.256%	11.102% qtr.
Allegheny Electric #175	10/12	3,745,000.00	10/31/84	10.315%	10.185% qtr.
Deseret G&T #211	10/12	13,725,000.00	10/20/84	10.285%	10.156% qtr.
Tennessee Telephone #80	10/13	1,223,000.00	10/13/84	9.815%	9.697% qtr.
East Kentucky Power #73	10/14	2,000,000.00	12/31/16	10.798%	10.565% qtr.
East Kentucky Power #140	10/14	1,200,000.00	12/31/16	10.798%	10.565% qtr.
East Kentucky Power #188	10/14	4,479,000.00	12/31/16	10.798%	10.565% qtr.
*Central Electric Power #131	10/14	60,000.00	10/14/84	9.805%	9.688% qtr.
New Hampshire Electric #192	10/15	1,008,000.00	12/31/16	10.948%	10.802% qtr.
Corn Belt Power #138	10/15	800,000.00	12/31/16	10.948%	10.802% qtr.
Cajun Electric #147	10/15	38,200,000.00	12/31/16	10.948%	10.802% qtr.
Plains Electric G&T #215	10/15	1,417,000.00	12/31/16	10.948%	10.802% qtr.
*Brazos Electric #108	10/15	2,626,000.00	10/15/84	9.965%	9.844% qtr.
*Brazos Electric #144	10/15	951,000.00	10/15/84	9.965%	9.844% qtr.
°Cooperative Power #130	10/15	12,000,000.00	12/31/13	10.905%	10.760% qtr.
°Cooperative Power #5	10/15	4,000,000.00	12/31/13	10.905%	10.760% qtr.
°Cooperative Power #130	10/15	8,000,000.00	12/31/13	10.905%	10.760% qtr.
*Oglethorpe Power #74	10/15	12,520,000.00	12/31/12	10.892%	10.748% qtr.
*East Kentucky Power #140	10/15	670,000.00	12/31/14	10.915%	10.770% qtr.
*Seminole Electric #141	10/16	3,352,000.00	10/16/84	10.125%	10.000% qtr.
*Associated Electric #132	10/17	15,500,000.00	12/31/14	11.080%	10.931% qtr.
Plains Electric G&T #158	10/17	5,950,000.00	12/31/14	11.080%	10.931% qtr.
°New Hampshire Electric #192	10/18	428,000.00	12/31/16	11.099%	10.949% qtr.
°New Hampshire Electric #192	10/18	1,755,000.00	12/31/16	11.099%	10.949% qtr.
°New Hampshire Electric #192	10/18	973,000.00	12/31/16	11.099%	10.949% qtr.
Florence Telephone #40	10/18	344,000.00	12/31/16	11.099%	10.949% qtr.
*Western Illinois Power #99	10/19	55,061,000.00	12/31/12	10.919%	10.774% qtr.
*Soyland Power #105	10/19	61,085,000.00	12/31/12	10.919%	10.774% qtr.
Brazos Electric #108	10/20	480,000.00	10/20/84	9.945%	9.824% qtr.
Brazos Electric #230	10/20	2,333,000.00	10/20/84	9.945%	9.824% qtr.
Basin Electric #137	10/20	20,000,000.00	10/20/84	9.945%	9.824% qtr.
Seminole Electric #141	10/20	10,241,000.00	12/31/16	10.935%	10.789% qtr.
*S. Mississippi Electric #3	10/20	3,500,000.00	12/31/09	10.822%	10.679% qtr.
*Big Rivers Electric #58	10/20	4,407,000.00	10/20/85	10.305%	10.176% qtr.
*Big Rivers Electric #65	10/20	28,000.00	10/20/84	9.945%	9.824% qtr.
*Big Rivers Electric #91	10/20	1,790,000.00	10/20/85	10.305%	10.176% qtr.
*Big Rivers Electric #91	10/20	898,000.00	10/20/84	9.945%	9.824% qtr.
*Big Rivers Electric #136	10/20	193,000.00	10/20/84	9.945%	9.824% qtr.
*Big Rivers Electric #143	10/20	136,000.00	10/20/84	9.945%	9.824% qtr.
*Corn Belt Power #166	10/21	150,000.00	10/21/84	9.845%	9.727% qtr.
*Sugar Land Telephone #69	10/21	1,000,000.00	10/21/84	9.845%	9.727% qtr.
°Colorado Ute Electric #8	10/21	2,708,000.00	12/31/11	10.952%	10.806% qtr.
*United Power #139	10/21	1,550,000.00	12/31/14	10.982%	10.835% qtr.
*United Power #86	10/21	630,000.00	12/31/14	10.982%	10.835% qtr.
Big Rivers Electric #136	10/21	97,000.00	10/21/84	9.845%	9.727% qtr.

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
RURAL ELECTRIFICATION ADMINISTRATION (Cont'd)					
Big Rivers Electric #143	10/21	$ 618,000.00	10/21/84	9.845%	9.727% qtr.
Big Rivers Electric #179	10/21	17,600,000.00	10/21/84	9.845%	9.727% qtr.
*Corn Belt Power #166	10/21	150,000.00	12/31/14	10.982%	10.835% qtr.
*United Power #67	10/22	1,500,000.00	12/31/14	10.987%	10.840% qtr.
*United Power #129	10/22	4,500,000.00	12/31/14	10.987%	10.840% qtr.
*Colorado Ute Electric #78	10/22	900,000.00	10/22/85	10.395%	10.263% qtr.
*Deseret G&T #170	10/24	58,716,000.00	12/31/14	11.109%	10.959% qtr.
*Seminole Electric #141	10/24	2,122,000.00	12/31/14	11.109%	10.959% qtr.
°Basin Electric #137	10/25	15,000,000.00	12/31/14	11.109%	10.959% qtr.
Kamo Electric #209	10/25	1,079,000.00	12/31/16	11.122%	10.972% qtr.
Wabash Valley Power #206	10/25	140,000.00	10/25/84	9.995%	9.873% qtr.
Wolverine Electric #233	10/25	498,000.00	10/25/84	9.995%	9.873% qtr.
Basin Electric #137	10/25	23,710,000.00	10/25/84	9.995%	9.873% qtr.
*Southern Illinois Power #38	10/25	650,000.00	12/31/13	11.101%	10.951% qtr.
*Brookville Telephone #53	10/25	1,412,000.00	12/31/12	11.091%	10.941% qtr.
°United Power #6	10/27	5,700,000.00	12/31/13	11.216%	11.063% qtr.
°United Power #67	10/27	6,350,000.00	12/31/13	11.216%	11.063% qtr.
East River Electric #117	10/28	3,000,000.00	10/28/86	10.795%	10.653% qtr.
°East Kentucky Power #73	10/28	8,302,000.00	12/31/13	11.243%	11.089% qtr.
°East Kentucky Power #73	10/28	6,586,000.00	12/31/13	11.243%	11.089% qtr.
°East Kentucky Power #73	10/28	7,061,000.00	12/31/13	11.243%	11.089% qtr.
°East Kentucky Power #73	10/28	7,909,000.00	12/31/13	11.243%	11.089% qtr.
°M&A Electric #111	10/28	1,125,000.00	12/31/12	11.227%	11.074% qtr.
°M&A Electric #111	10/28	501,000.00	12/31/13	11.243%	11.089% qtr.
°M&A Electric #111	10/28	325,000.00	12/31/13	11.243%	11.089% qtr.
°M&A Electric #111	10/28	830,000.00	12/31/13	11.243%	11.089% qtr.
°M&A Electric #111	10/28	200,000.00	12/31/13	11.243%	11.089% qtr.
°M&A Electric #111	10/28	250,000.00	12/31/13	11.243%	11.089% qtr.
°M&A Electric #111	10/28	200,000.00	12/31/14	11.257%	11.103% qtr.
°M&A Electric #111	10/28	487,000.00	12/31/15	11.271%	11.117% qtr.
*Ponderosa Telephone #35	10/29	395,000.00	10/29/84	10.015%	9.893% qtr.
North Carolina Telephone #185	10/29	7,000,000.00	10/29/84	10.015%	9.893% qtr.
Colorado Ute Electric #168	10/29	12,000,000.00	10/29/84	10.015%	9.893% qtr.
Colorado Ute Electric #203	10/29	2,019,000.00	10/29/84	10.015%	9.893% qtr.
Basin Electric #137	10/29	20,000,000.00	10/29/84	10.015%	9.893% qtr.
Sunflower Electric #174	10/29	30,000,000.00	12/31/16	11.169%	11.017% qtr.
Cajun Electric #197	10/29	26,000,000.00	12/31/16	11.169%	11.017% qtr.
M&A Electric #111	10/29	1,490,000.00	12/31/16	11.169%	11.017% qtr.
°Sunflower Electric #174	10/29	25,000,000.00	12/31/14	11.144%	10.993% qtr.
°Sunflower Electric #174	10/29	10,000,000.00	12/31/15	11.157%	11.006% qtr.
°Sunflower Electric #174	10/29	35,000,000.00	12/31/15	11.157%	11.006% qtr.
°Sunflower Electric #174	10/29	15,000,000.00	12/31/15	11.157%	11.006% qtr.
*Big Rivers Electric #58	10/30	945,000.00	10/30/85	10.475%	10.341% qtr.
*Big Rivers Electric #91	10/30	305,000.00	10/30/85	10.475%	10.341% qtr.
*East Kentucky Power #73	10/30	19,184,000.00	12/31/12	11.007%	10.860% qtr.
*Seminole Electric #141	10/30	879,000.00	12/31/14	11.038%	10.890% qtr.
*Allegheny Electric #93	10/31	2,445,000.00	10/31/84	9.975%	9.854% qtr.
*S. Mississippi Electric #171	10/31	24,210,000.00	12/31/14	11.038%	10.890% qtr.
*Arkansas Electric #142	10/31	2,837,000.00	10/31/84	9.975%	9.854% qtr.
*Gulf Telephone #50	10/31	168,285.00	11/1/84	9.975%	9.854% qtr.
*Southern Illinois Power #38	10/31	2,920,000.00	12/31/11	10.685%	10.546% qtr.
*Basin Electric #87	10/31	332,000.00	12/31/14	11.038%	10.890% qtr.
*Basin Electric #88	10/31	777,000.00	12/31/12	11.007%	10.860% qtr.
*Southern Illinois Power #38	10/31	500,000.00	12/31/14	11.038%	10.890% qtr.
*San Miguel Electric #110	10/31	3,000,000.00	12/31/14	11.038%	10.890% qtr.
*Arkansas Electric #142	10/31	2,837,000.00	12/31/14	11.038%	10.890% qtr.
SMALL BUSINESS ADMINISTRATION					
Small Business Investment Company Debentures					
Northland Capital Corp.	10/20	200,000.00	10/1/85	10.345%	
Northland Capital Corp.	10/20	200,000.00	10/1/87	10.535%	
Round Table Cap. Corp.	10/20	600,000.00	10/1/89	10.665%	
Wood River Cap. Corp.	10/20	4,000,000.00	10/1/89	10.665%	
Bando-McGlocklin Inv. Co.	10/20	1,500,000.00	10/1/92	10.705%	
Brittany Cap. Corp.	10/20	300,000.00	10/1/92	10.705%	
Capital Marketing Corp.	10/20	2,000,000.00	10/1/92	10.705%	

*maturity extension
°early extension

OCTOBER 1982 ACTIVITY

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
Small Business Investment Company Debentures (Cont'd)					
European Dev. Cap. Corp.	10/20	$ 1,000,000.00	10/1/92	10.705%	
SBI Cap. Corp.	10/20	500,000.00	10/1/92	10.705%	
Tidewater Industrial Cap. Corp.	10/20	300,000.00	10/1/92	10.705%	
Unicorn Ventures, Ltd.	10/20	500,000.00	10/1/92	10.705%	
State & Local Development Company Debentures					
Jackson Local Dev. Corp.	10/6	38,000.00	10/1/97	11.829%	
St. Louis Local Dev. Co.	10/6	42,000.00	10/1/97	11.829%	
CCD Business Dev. Corp.	10/6	46,000.00	10/1/97	11.829%	
Toledo Econ. Planning Council	10/6	83,000.00	10/1/97	11.829%	
Lynn Cap. Inv. Corp.	10/6	93,000.00	10/1/97	11.829%	
City-Wide Sm. Bus. Dev. Corp.	10/6	95,000.00	10/1/97	11.829%	
VERD-ARK-CA Dev. Corp.	10/6	101,000.00	10/1/97	11.829%	
St. Louis Local Dev. Corp.	10/6	105,000.00	10/1/97	11.829%	
Com. Dev. Corp. of Ft. Wayne	10/6	63,000.00	10/1/02	11.815%	
St. Louis County Local Dev. Co.	10/6	91,000.00	10/1/02	11.815%	
Lynn Cap. Inv. Corp.	10/6	126,000.00	10/1/02	11.815%	
Plymouth Industrial Dev. Corp.	10/6	160,000.00	10/1/02	11.815%	
Eastern Maine Dev. District	10/6	163,000.00	10/1/02	11.815%	
Ocean State Bus. Dev. Auth.	10/6	172,000.00	10/1/02	11.815%	
Ocean State Bus. Dev. Auth.	10/6	223,000.00	10/1/02	11.815%	
Androscoggin Valley Reg. Pl. Com.	10/6	256,000.00	10/1/02	11.815%	
Greater Bakersfield L.D.C.	10/6	263,000.00	10/1/02	11.815%	
Long Island Dev. Corp.	10/6	315,000.00	10/1/02	11.815%	
Pawtuckett Local Com. & I.D.C.	10/6	315,000.00	10/1/02	11.815%	
Los Angeles L.D.C., Inc.	10/6	500,000.00	10/1/02	11.815%	
Ocean State Bus. Dev. Auth.	10/6	34,000.00	10/1/07	11.821%	
Washington, D.C. Loc. Dev. Co.	10/6	47,000.00	10/1/07	11.821%	
Wisconsin Bus. Dev. Fin. Corp.	10/6	36,000.00	10/1/07	11.821%	
Los Angeles L.D.C. Inc.	10/6	122,000.00	10/1/07	11.821%	
Tucson Local Dev. Corp.	10/6	173,000.00	10/1/07	11.821%	
Wisconsin Bus. Dev. Fin. Corp.	10/6	184,000.00	10/1/07	11.821%	
Bay Area Employment Dev. Co.	10/6	230,000.00	10/1/07	11.821%	
Washington, D.C. Loc. Dev. Co.	10/6	261,000.00	10/1/07	11.821%	
La Habra Local Dev. Co., Inc.	10/6	500,000.00	10/1/07	11.821%	
Los Angeles L.D.C., Inc.	10/6	500,000.00	10/1/07	11.821%	
TENNESSEE VALLEY AUTHORITY					
Seven States Energy Corporation					
Note A-83-1	10/29	327,569,918.02	1/31/83	8.308%	
DEPARTMENT OF TRANSPORTATION					
National Railroad Passenger Corporation					
*Amtrak #21	10/1	200,000,000.00	1/3/83	7.980%	
*Amtrak #29	10/1	600,000,000.00	1/3/83	7.980%	
Section 511					
Missouri-Kansas-Texas R.R.	10/21	15,000,000.00	4/30/90	10.709%	

* maturity extension

FEDERAL FINANCING BANK
October 1982 Commitments

BORROWER	AMOUNT	GUARANTOR	COMMITMENT EXPIRES	MATURITY
Ashland, KY	$ 400,000.00	HUD	2/15/83	2/15/88
Albany Ind. Dev. Agency	3,000,000.00	HUD	7/1/83	7/1/03

FEDERAL FINANCING BANK HOLDINGS
(in millions)

Program	September 30, 1982	October 31, 1982	Net Change 10/1/82-10/31/82
On-Budget Agency Debt			
Tennessee Valley Authority	$ 12,285.0	$ 12,460.0	$ 175.0
Export-Import Bank	13,953.9	13,953.9	-0-
NCUA-Central Liquidity Facility	130.1	145.0	15.0
Off-Budget Agency Debt			
U.S. Postal Service	1,221.0	1,221.0	-0-
U.S. Railway Association	194.9	191.5	-3.4
Agency Assets			
Farmers Home Administration	53,736.0	53,661.0	-75.0
DHHS-Health Maintenance Org.	131.0	131.0	-0-
DHHS-Medical Facilities	145.7	145.7	-0-
Overseas Private Investment Corp.	21.5	21.5	-0-
Rural Electrification Admin.-CBO	3,123.7	3,123.7	-0-
Small Business Administration	58.1	57.3	-.8
Government-Guaranteed Loans			
DOD-Foreign Military Sales	11,435.8	11,630.7	194.9
DEd.-Student Loan Marketing Assn.	5,000.0	5,000.0	-0-
DOE-Geothermal Loans	36.6	40.9	4.3
DOE-Non-Nuclear Act (Great Plains)	340.0	378.5	38.5
DHUD-Community Dev. Block Grant	117.0	119.0	2.0
DHUD-New Communities	33.5	33.5	-0-
DHUD-Public Housing Notes	1,624.3	1,659.0	34.8
General Services Administration	420.5	420.5	-0-
DOI-Guam Power Authority	36.0	36.0	-0-
DOI-Virgin Islands	29.5	29.5	-0-
NASA-Space Communications Co.	757.8	774.3	16.5
Rural Electrification Admin.	16,281.5	16,600.0	318.4
SBA-Small Business Investment Cos.	712.0	721.0	9.0
SBA-State/Local Development Cos.	48.4	53.7	5.3
TVA-Seven States Energy Corp.	1,258.0	1,233.6	-24.3
DOT-Amtrak	855.4	855.4	-0-
DOT-Section 511	193.0	190.0	-3.2
DOT-WMATA	177.0	177.0	-0-
TOTALS*	$ 124,357.3	$ 125,064.2	$ 707.0

*figures may not total due to rounding

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
Thursday, February 3, 1983

CONTACT: Michael Brown
(202)376-0560

THE PRESIDENT REAGAN MEDAL

Treasury Secretary Donald T. Regan presented President Reagan with his official Presidential medals, struck by the United States Mint, in an Oval Office ceremony this afternoon. Joining in the presentation were Donna Pope, Director of the U.S. Mint, and Miss Elizabeth Jones, Chief Sculptor- Engraver of the United States. The medals are part of the Mint's historic tradition of striking a commemorative medal for each President.

The three-inch bronze Presidential medal and the miniature one and 5/16th inch bronze medal will be added to the Mint's National Medals Program and will be available for purchase by the public. Director Pope emphasized, "this is a self-supporting and profitable program with no tax dollars expended."

Miss Elizabeth Jones designed and modeled the medal. The obverse features an impressionistic-style portrait of President Reagan developed from photographs furnished by the White House. The incription, RONALD REAGAN, appears along the top border and PRESIDENT OF THE UNITED STATES along the lower border. The artist's name, E.A.B. Jones, appears on the base of the portrait.

The reverse design was suggested by First Lady Nancy Reagan as representative of the President's attachment to mountains. It features Half Dome, a mountain in Yosemite National Park. The quotation in the upper field is, "LET US RENEW OUR FAITH AND OUR HOPE. WE HAVE EVERY RIGHT TO DREAM HISTORIC DREAMS." It was taken from the President's Inaugural Address. "INAUGURATED JANUARY 20, 1981" follows the quotation. The artist's initials, E.J., appear along the right lower border and YOSEMITE NATIONAL PARK along the left lower border.

The two medals will be available at all Mint sales outlets and by mail order. The 3-inch medal retails for $10.00 over-the-counter and $10.75 by mail order. The minature medal retails for 75 cents over-the-counter and $1.00 by mail order. All mail orders for the President Reagan medals should be sent to:

Bureau of the Mint
55 Mint Street
San Francisco, CA 94175

(more)

R-2015

OVER-THE-COUNTER SALES AT:

Philadelphia Mint
Independence Mall,
5th and Arch Street
Philadelphia, PA

Denver Mint
320 Colfax Avenue
Denver, CO

San Francisco Old Mint
88 Fifth Street
(Fifth & Mission)
San Francisco, CA

Department of the Treasury
15th Street & Pennsylvania Ave., N.W.
Washington, D.C.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE February 2, 1983

RESULTS OF AUCTION OF 10-YEAR NOTES

The Department of the Treasury has accepted $4,501 million of $10,343 million of tenders received from the public for the 10-year notes, Series A-1993, auctioned today. The notes will be issued February 15, 1983, and mature February 15, 1993.

The interest rate on the notes will be 10-7/8%. The range of accepted competitive bids, and the corresponding prices at the 10-7/8% interest rate are as follows:

	Bids	Prices
Lowest yield	10.92%	99.730
Highest yield	10.96%	99.491
Average yield	10.94%	99.611

Tenders at the high yield were allotted 42%.

TENDERS RECEIVED AND ACCEPTED (In Thousands)

	Received	Accepted
Boston	$ 24,603	$ 11,323
New York	8,608,896	3,950,406
Philadelphia	16,700	6,700
Cleveland	51,693	43,693
Richmond	42,970	15,650
Atlanta	31,978	22,978
Chicago	904,752	222,512
St. Louis	67,829	61,539
Minneapolis	17,299	12,219
Kansas City	25,901	24,801
Dallas	7,423	6,263
San Francisco	541,948	122,248
Treasury	1,029	1,029
Totals	$10,343,021	$4,501,361

The $4,501 million of accepted tenders includes $1,012 million of noncompetitive tenders and $3,489 million of competitive tenders from the public.

In addition to the $4,501 million of tenders accepted in the auction process, $20 million of tenders was awarded at the average price to Federal Reserve Banks as agents for foreign and international monetary authorities. An additional $650 million of tenders was also accepted at the average price from Government accounts and Federal Reserve Banks for their own account in exchange for maturing securities.

R-2016

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE UPON DELIVERY
EXPECTED AT 9:30 A.M.
Thursday, February 3, 1983

TESTIMONY OF THE HONORABLE DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
SENATE FINANCE COMMITTEE

Mr. Chairman and Members of the Committee:

It is a pleasure to meet with you today and to discuss the Administration's 1984 budget proposals. The development of a sound fiscal policy was one of the central objectives of the Reagan Administration when it came into office two years ago. For too long a time Americans had watched the share of GNP accounted for by Federal spending and taxes move upward. As the government siphoned off resources from the private sector and the money supply expanded, economic activity stagnated and inflation soared.

In February 1980 the Administration put before Congress a four point plan to revitalize the economy. Our program included spending restraint, tax reductions, regulatory reform, and support of the Federal Reserve's efforts to attain gradual, steady reduction in the rate of monetary growth.

The transition to a noninflationary environment has been somewhat more difficult than anticipated. We have seen two years of serious economic recession as a result of the inflation/tax spiral.

However, the worst is now over. There has been clear progress on inflation, and consumer price growth has dropped dramatically from 12.4 percent in 1980 to 3.9 percent in 1982. Interest rates are down from peak levels of 21-1/2 percent on the prime in December 1980 to 11 percent currently, and the stock market last year made new highs. Indicators such as housing, inventories, and real income show the economy is poised for recovery. Alongside these favorable developments, there remains distressingly high unemployment.

R- 2017

- bringing inflation under control;
- shifting the composition of activity away from government spending toward more productive endeavors in the private sector;
- providing an environment which would reward innovation, work effort, saving and investment, and in which free-market forces could operate effectively.

Over the past two years we have seen evidence that the Administration's program is working. The fundamental elements of recovery are now largely in place. Inflation has been brought under control. Interest rates are coming down, as shown in Chart II. Real wage growth is being restored. In addition, there have been other improvements -- notably in productivity growth and saving behavior -- which mark a shift away from the problems that contributed to sluggish economic performance in recent years.

Within this framework of very significant achievements, there remains the fact that the economy has been in recession and unemployment is high. The unemployment rate of 10.8 percent in December is, of course, a matter of great concern. The President has indicated in his State of the Union Message that he will be submitting special legislation to help deal with the problem.

The Current State of the Economy

The economy now stands poised for recovery. In fact, the recovery may well already be underway at this moment. It has been much longer in coming than we, or for that matter nearly all forecasters, had expected.

The delay occurred primarily because of the persistence of high interest rates and because of developments in the international sphere. On the international front, the economies of our leading trading partners continued to weaken. Weakness among all the industrialized nations was self-reinforcing. Furthermore, the financial difficulties of some of the newly industrializing nations had adverse impacts on economic activity here. These forces, combined with a general hesitancy on the part of the consumer, led to another round of inventory cutting in the second half of 1982 and delayed the expected turnaround of the economy.

The Outlook for the Economy

A vigorous recovery of the type outlined would be most welcome. It would certainly help ease the Nation's budgetary problems. However, we recognize that the serious problems still confronting us may well hold growth during the next year or two below the typical recovery pattern.

- Our overall trade balance is likely to register further marked deterioration in the coming year.

- Real interest rates may persist at high levels, though remaining below those prevailing a year ago.

- The economy is in the process of undergoing marked structural change. Some of our industries may not quickly regain the vitality they experienced in the 1950's and 1960's. The shift of resources to emerging industries will take time.

- Most fundamentally, we are not yet fully out of the inflationary woods, and we cannot afford to direct monetary and fiscal policy toward excessively rapid economic expansion.

For these reasons, the Administration is forecasting fairly modest real growth at a 3.1 percent rate during the four quarters of 1983, rather than the typical recovery growth rate of about twice that much, though certainly we would welcome a stronger recovery. Growth is expected to pick up modestly to the 4 percent range in 1984 and the years beyond.

Policies for the Recovery

In setting policy for the remainder of the 1980's, we must recognize what we must <u>not</u> do. We no longer have the freedom of action to revert back to the overly stimulative monetary and fiscal policies pursued at times in the past, for these would surely lead to a resurgence of inflationary pressures and a new round of rising interest rates. Further, we must not reverse the fundamental tax restructuring put in place in 1981, for this was designed to provide the noninflationary incentives without which the private sector would continue to wither.

Legislation providing for the U.S. share of the increase in IMF resources will be submitted in the near future and I urge prompt approval by the Congress.

Monetary Policy

In addition to policies aimed at facilitating structural changes within the economy, we must maintain steady monetary and fiscal policies directed at reinvigorating economic activity. Steady, predictable money supply growth at a noninflationary pace has been, and continues to be, one of the major goals of the Administration's economic program. The Federal Reserve's efforts to achieve that goal have been complicated by a number of factors, such as far-reaching institutional changes in the banking and thrift industries. Nevertheless, the Fed has generally been successful, albeit in a somewhat erratic fashion.

Monetary policy faced a difficult and uncertain situation during much of the last year. Rapid institutional change in the form of new money market instruments blurred the boundaries between the various aggregates and made the achievement of any target rates of growth unusually difficult. There is also some indication that the recession may have led to an increased demand for liquidity and precautionary balances. In 1982, growth in monetary velocity -- the rate at which money is used -- turned negative for the first time in nearly three decades. Under the unusual economic and institutional circumstances of 1982, some temporary offset in the form of above-target rates of monetary growth was probably desirable.

The Federal Reserve's efforts to slow money growth have been accompanied by some volatile short-run swings. Growth in M1 was actually negative on a 13-week basis by mid-summer of last year, and then soared to the double-digit range by the end of the year. This recent acceleration has caused some observers to conclude that the fight against inflationary money growth has been abandoned. That is not true. Both the Administration and the Federal Reserve remain committed to the long-run goal of providing money growth at a noninflationary pace consistent with a steady and sustainable expansion of economic activity.

Fiscal Policy

The objectives of our fiscal policy upon coming to office two years ago were two-fold. First, we believed and still believe it was imperative to correct the disincentives to economic performance that had been built into the tax structure over the years. These disincentives arose in large measure, not by design, but through the interaction of a high rate of inflation with a progressive tax system and historical cost accounting of depreciable assets. Second, it was equally

hardly ask honest taxpayers to pick up this additional burden. Repealing withholding at this time would also send a message that the government does not take seriously the major effort initiated last year to insure better compliance with the tax laws in general.

Last year we were relatively successful in working with the Congress to achieve our goals of tax reform, but we were less successful in the area of outlay control. A major portion of the savings we had proposed in our original budget did not receive favorable action. This, along with much weaker economic activity than expected, has left us facing the prospect of large deficits even as the economy recovers.

The proposals in the FY-1984 Budget are directed at the crucial task of restoring noninflationary economic growth. This requires the preservation of the investment and work incentives provided by the tax reforms of 1981 and a reduction in the high deficits and interest rates which lie ahead unless corrective action is taken to bring government outlays under control.

The tax reforms already enacted will enable us to make good progress in rebuilding and modernizing America's plant and equipment as the recovery progresses. Incentives are in place to encourage saving and investment and to lower the cost of new machinery and structures. Taxes on American labor are coming down. These reforms will lead to a more productive, more competitive United States. The capital formation program will be financed by higher levels of personal saving, more generous capital consumption allowances, and higher retained earnings as profits recover from the current slump. These elements, plus state and local budget surpluses, form the Nation's savings pool.

Spending reduction will contribute to the recovery, and the recovery will contribute to deficit reduction. The deficit will fall as the economy advances, particularly if the recovery is a vigorous one. A strong recovery with 1-1/3 percent more real growth per year than in our forecast would bring the budget to near balance by 1988, provided we also curb the growth of Federal outlays.

However, if we fail to bring spending under control and if recovery is slow, we will face a deficit problem which is larger and longer-lasting than we can afford. In such case, the deficit could run in the range of 6 to 7 percent of GNP each year through 1988. Our tax reforms were designed to raise the private savings share, but still we would face

Our Budget Proposals

Spending reduction is crucial. Unfortunately, it has been difficult to achieve because of the built-in momentum of Federal spending programs. Consequently, we are proposing strong medicine. We, like a great many other nations in the world, have tried to live beyond our means. Now we must bring our spending into line with our productive capacity and strengthen the private sector which produces our national wealth.

The deficit reduction program that we propose contains four basic elements.

- o The first is a freeze on 1984 outlays to the extent possible. Total outlays shall be frozen in real terms in 1984. The 6-month freeze on COLAs, as recommended by the Social Security Commission, is to be extended to other indexed programs. There will be a 1-year freeze on pay and retirement of Federal workers, both civilian and military. Many workers in the private sector have accepted freezes in their pay. Federal workers can also make a sacrifice, which may serve as an example for sectors of the economy that have not yet recognized the need for moderation in wage demands. As a final item of freeze, outlays for a broad range of nonentitlement progams will be held at 1983 levels.

- o The second element of our budgetary program contains measures to control the so-called "uncontrollable." Laws have been so written that Federal payments are automatic to all those declared eligible. We plan a careful review of all such programs, taking special care to protect those truly in need.

- o The third element is a cutback of $55 billion in defense outlays from original plans.

- o Fourth is a set of proposals involving the revenue side of the budget, described below.

We are projecting receipts for the current year (fiscal year 1983) of $597.5 billion. For fiscal year 1984 we expect receipts to be $659.7 billion. The 1983 figure represents a decline of $20.3 billion from the fiscal year 1982 total of $617.8 billion. This decline, and indeed the absence of an increase in receipts in the range of $50-$70 billion, is explained in large part by the recession. As I have already explained, our economic projections throughout the remainder of the recovery period are cautious. If real GNP grows at a faster rate than we have projected, then receipts for the current fiscal year, as well as for subsequent years, will be somewha higher than we are now projecting.

a cap on the amount of employer-paid health insurance premiums that may be excluded from employees' taxable incomes, and a limited exclusion from tax for earnings on savings set aside for higher education expenses.

Last, the President has included in his budget message a contingency tax plan designed as a stand-by insurance program to insure additional tax revenue if deficits are projected to exceed two and one-half percent of GNP in 1986.

In addition to these eight specific tax proposals, the President has directed Treasury to undertake a careful study of the current income tax structure. We will be searching for ways to simplify the tax system, to make it fairer, and to remove tax obstacles to economic growth and expanding employment.

Let me now discuss some of the details of each of these proposals.

Social Security. As the President made clear in his State of the Union Address, the Administration strongly supports the bipartisan plan recommended by the National Commission on Social Security Reform. Although this Committee will be taking up all aspects of the proposal, I will concentrate today on just the tax aspects of the bipartisan plan. Three major Social Security tax changes are proposed.

First, there will be a slight acceleration of the scheduled increase in the payroll tax rate in 1984 and then again in 1988 and 1989. For 1984, an income tax credit will be provided to refund the increase for employees. Second, beginning in 1984 the self-employment tax rate will be made comparable to the combined employer-employee tax rate, with one-half of the new self-employment rate being deductible as a business cost in calculating taxable income. Third, single taxpayers with more than $20,000 and married couples with more than $25,000 of adjusted gross income from non-social security sources will be required to include 50 percent of their Social Security benefits in adjusted gross income subject to the Federal income tax. Any technical problem in designing the income tax changes will be worked out within the spirit of the bipartisan compromise.

Further, beginning in 1984, mandatory coverage will be extended to all new Federal employees and employees of nonprofit organizations. Also, State and local governments currently paticipating in the system will no longer be allowed to withdraw.

Together with the recommended changes in benefits, these tax changes will provide the necessary revenues to assure adequate funding for the Social Security system for many

For a three-year period beginning in 1983, the Secretary of Housing and Urban Development may designate up to 75 small areas as enterprise zones. No more than 25 zones will be designated each year. For zones designated in 1983, the tax incentives will become effective January 1, 1984. The enterprise zone tax incentives are estimated to reduce receipts by $0.1 billion in 1984, $0.4 billion in 1985, $0.8 billion in 1986.

The Administration also is reintroducing a proposal to allow taxpayers a credit against their income taxes equal to 50 percent of tuition costs for each child in a private elementary or secondary school. The provisions of this proposal are identical to those contained in the Senate Finance Committee bill of last year except that the income range over which the credit will phase out is $40,000 - $60,000 of adjusted gross income rather than $40,000 - $50,000 of adjusted gross income. The maxium credit per child would be $100 in 1983, $200 in 1984 and $300 in 1985 and thereafter. The Administration supports the strong anti-discrimination provisions passed by the Senate Finance Committee last year.

This proposal would be effective for tuition expenses paid on or after August 1, 1983. The proposal is estimated to reduce receipts by $0.2 billion in 1984, $0.5 billion in 1985, and $0.8 billion in 1986.

New Tax Initiatives. There are also three major new tax initiatives in this year's Budget. First, to help the long-term unemployed find meaningful jobs in the private sector, the Administration proposes a new tax credit for employers who hire individuals after they have exhausted their regular and extended unemployment insurance benefits. The tax credit is part of a plan to modify the present program for Federal Supplemental Compensation (FSC), turning that program into an effective hiring incentive. Rather than simply offering additional payments to those already out of work for a long period, this proposal will allow job seekers to convert FSC benefits to job vouchers they may offer to prospective employers as a hiring incentive. When the employee is hired, these vouchers entitle the employer to a credit against taxes, including their unemployment insurance taxes. After six months, the option to receive FSC benefits will end, but the tax incentives for hiring the long-term unemployed will continue until April 1984. The value of the tax credit will be equal to the benefits available under the FSC program. The proposed tax credit is estimated to reduce receipts by a negligible amount in 1983, $0.2 billion in 1984, $0.2 billion in 1985, and $0.1 billion in 1986.

The Administration also proposes to limit the amount of employer-paid health insurance premiums that may be excluded purpose will be assessed a penalty, except in the case of the child's death or when the savings are needed to pay for certain unusual medical expenses incurred by the child.

In order to encourage families to begin saving early for a child's higher education, deposits may be placed in these special savings accounts on behalf of any dependent children under the age of 18. In no case may an account be kept open for a child over the age of 25.

The following example illustrates how the exclusion from tax for earnings deposited in these accounts will help families set aside funds to enroll their children in colleges or universities of their choice. For a family with about $30,000 of income and making maximum contributions to accounts earning 10 percent per annum for two children, the tax reduction will be about $50 in the first year, $350 in the sixth year, and about $800 in the tenth year. Over the full 10 years, an additional $4,800 would be available to meet the qualified education expenses of the family's children.

If, in a future year, the taxpayer's adjusted gross income rises above $40,000, he will be eligible only for reduced deposit amounts, but the exclusion of income on previous deposits still will be allowed in full.

This exclusion for earnings on savings set aside for higher education is proposed to be effective January 1, 1984. It is estimated to reduce receipts by a negligible amount in 1984, $0.1 billion in 1985 and $0.2 billion in 1986.

Contingency Tax. Finally, the President has proposed a contingency tax plan designed to raise revenues of about 1 percent of GNP in the event that, after Congress has adopted the Administration's spending reduction proposals and structural reforms, there is insufficient economic growth to reduce the deficit below 2-1/2 percent of GNP. The contingency tax plan would go into effect on October 1, 1985, provided that the economy is growing on July 1, 1985 and the forecasted deficit for fiscal year 1986 exceeds 2-1/2 percent of GNP. The contingency tax plan is an insurance program. It is important to have a plan in place so that everyone will know that we will not tolerate a string of deficits that would exceed 2-1/2 percent of GNP. Chart VI shows the effect on the deficit that the contingency tax would have if it were implemented. It also shows how the budget picture would be altered by a much stronger expansion. The high growth deficit path shown reflects the assumption that real GNP increases 1-1/3 percentage points faster than in the official forecast path, starting with FY-1983. Such growth would be in line with economic performance from the end of 1960 to late 1966.

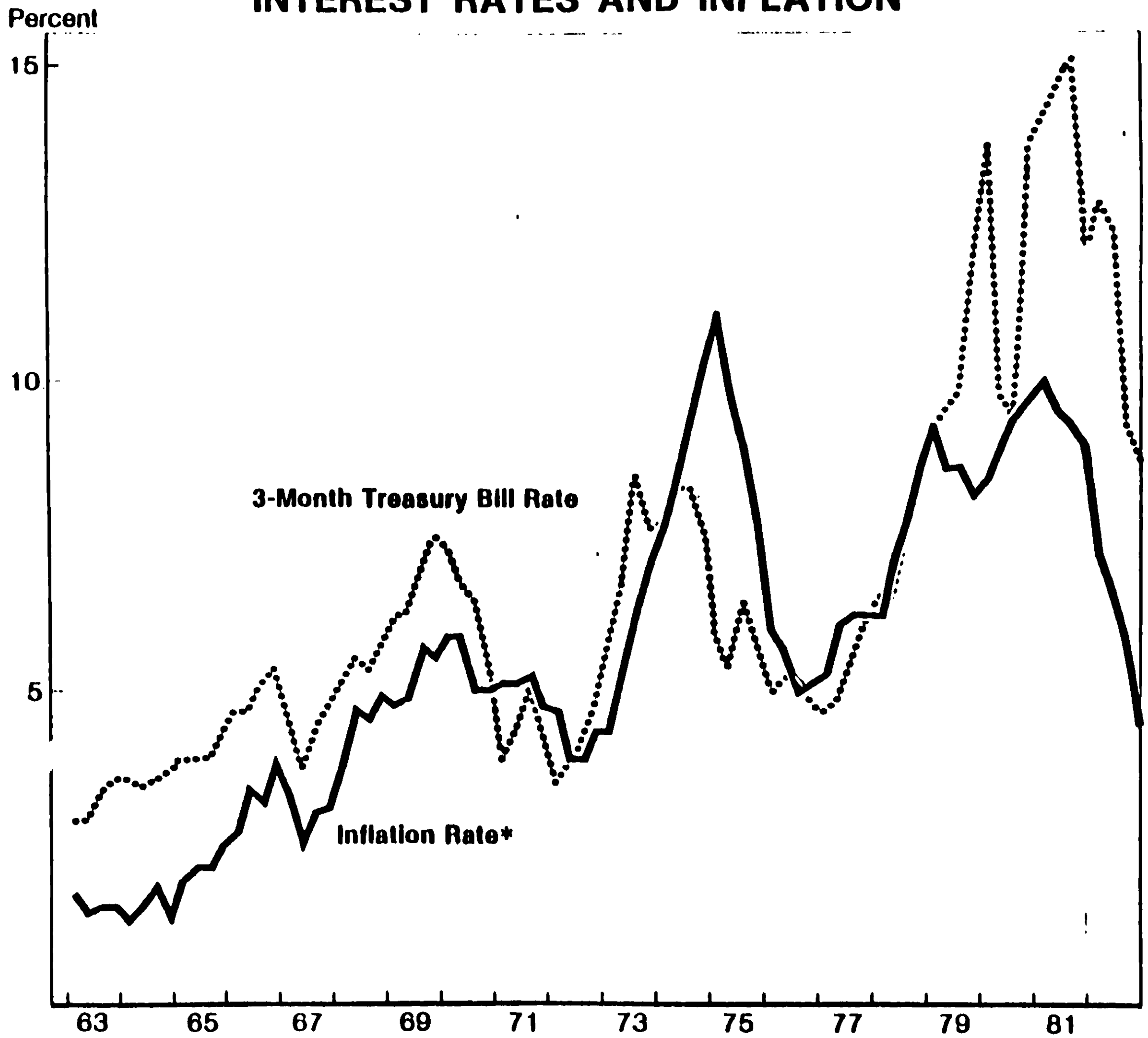
Conclusion

If all of the Administration's budget saving proposals are enacted, we will reduce the projected deficits by a total of $580 billion over the next 5 years, or by $2,400 for every man, woman, and child in the United States. The deficit as a share of GNP will be down to about 2-1/2 percent in 1988 from the 6-1/2 percent we expect this year. Total outlays will grow by only 1.9 percent per year in real terms over the next 5 years, compared with a bloated 3.9 percent real growth between 1977 and 1981.

We are confident that the deficit reduction program contained in this realistic budget is the right program for the economy at this critical juncture. The most important signals we can send the economy are spending restraint, deficit restraint, and a commitment to noninflationary economic growth throughout the decade. This is the program we are recommending. Together with the Congress, we can make it work.

Chart I

INTEREST RATES AND INFLATION

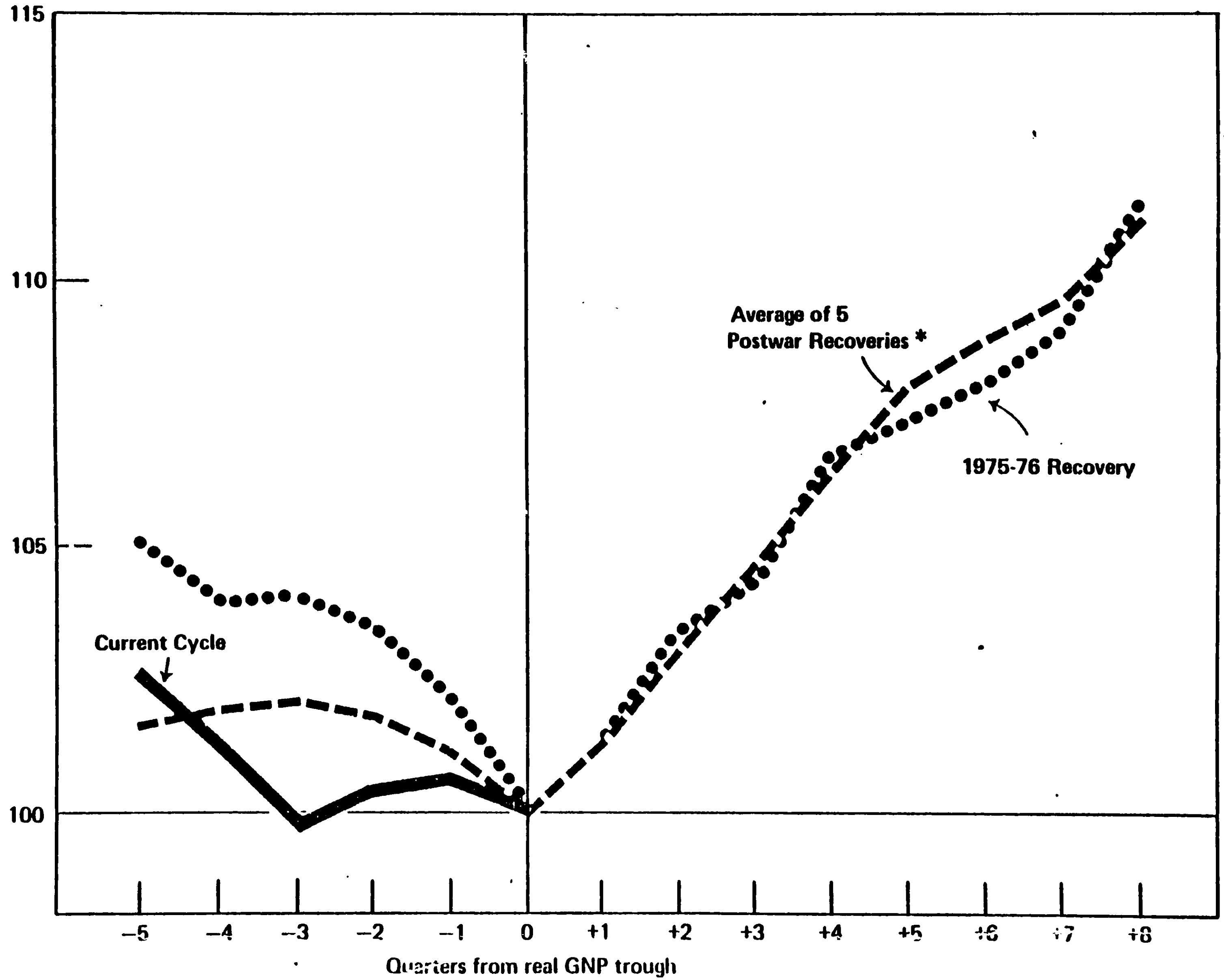


* Growth from year earlier in GNP deflator.
Plotted quarterly.

Chart III

THE PATH OF POSTWAR ECONOMIC RECOVERIES

Real GNP trough = 100



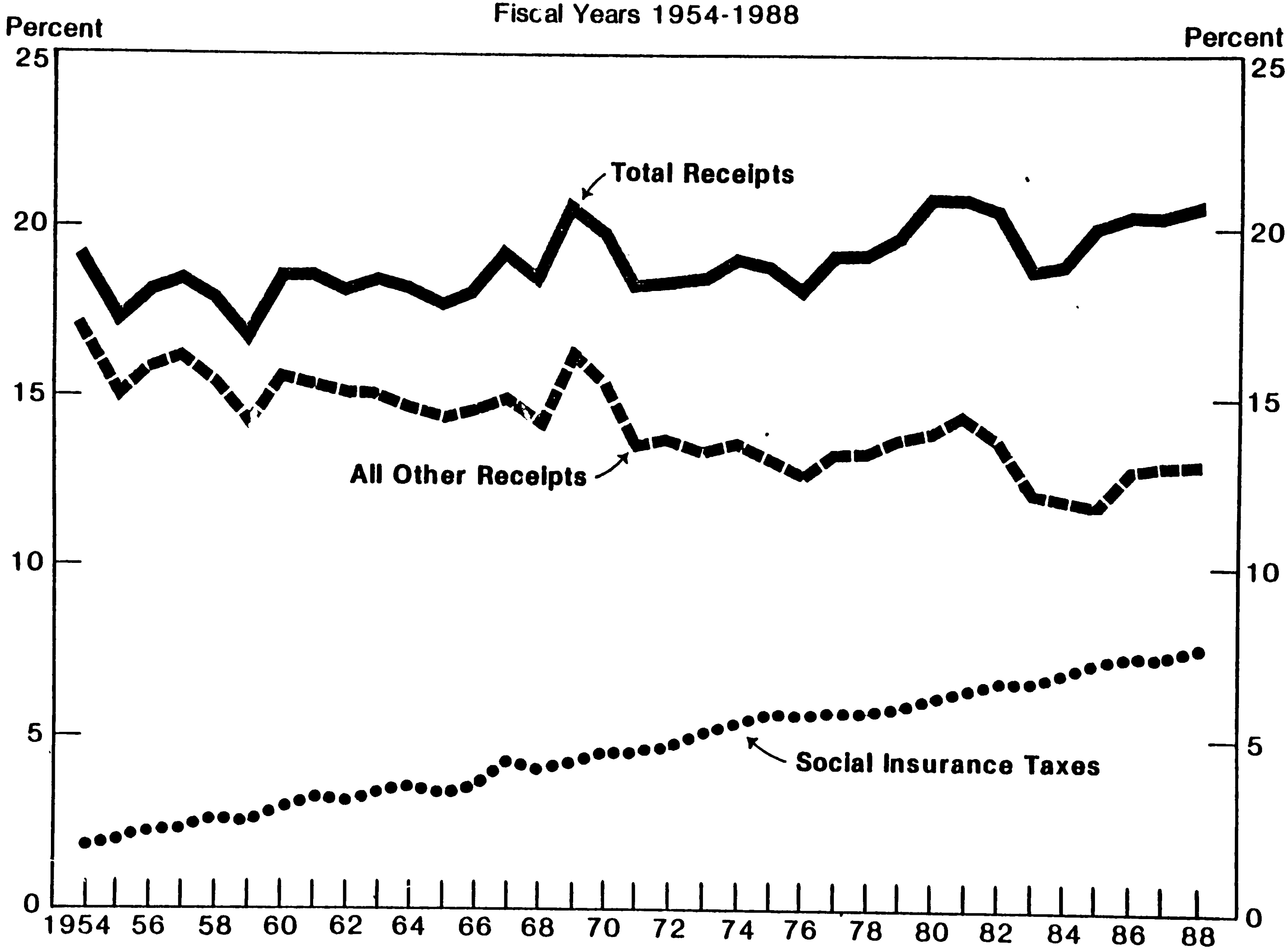
* Postwar recoveries excluding the Korean War period and the short-lived 1980-81 recovery.

January 25, 1983-A210

Chart V

UNIFIED BUDGET RECEIPTS AS A PERCENT OF GNP *

Fiscal Years 1954-1988



* Receipts include contingency taxes.

January 28, 1983-A215

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE February 3, 1983

RESULTS OF AUCTION OF 29-3/4-YEAR TREASURY BONDS
AND SUMMARY RESULTS OF FEBRUARY FINANCING

The Department of the Treasury has accepted $ 3,502 million of $ 6,197 million of tenders received from the public for the 10-3/8% 29-3/4-year Bonds of 2007-2012, auctioned today. The bonds will be issued February 15, 1983, and mature November 15, 2012.

The range of accepted competitive bids was as follows:

	Bids	Prices
Lowest yield	10.98%	94.650
Highest yield	11.05%	94.071
Average yield	11.01%	94.401

Tenders at the high yield were allotted 56%.

TENDERS RECEIVED AND ACCEPTED (In Thousands)

Location	Received	Accepted
Boston	$ 6,155	$ 6,155
New York	5,445,442	3,129,622
Philadelphia	3,060	3,060
Cleveland	4,228	3,348
Richmond	11,162	11,162
Atlanta	21,039	17,049
Chicago	292,579	150,079
St. Louis	55,364	51,144
Minneapolis	7,239	7,019
Kansas City	9,037	8,037
Dallas	1,119	1,119
San Francisco	340,329	114,289
Treasury	180	180
Totals	$6,196,933 a/	$3,502,263

a/ Excepting $730 million above the original issue discount yield limit of 11.21%.

The $ 3,502 million of accepted tenders includes $ 655 million of non-competitive tenders and $ 2,847 million of competitive tenders from the public.

In addition to the $ 3,502 million of tenders accepted in the auction process, $439 million of tenders were accepted at the average price from Government accounts and Federal Reserve Banks for their own account in exchange for maturing securities.

SUMMARY RESULTS OF FEBRUARY FINANCING

Through the sale of the three issues offered in the February financing, the Treasury raised approximately $9.2 billion of new money and refunded $8.0 billion of securities maturing February 15, 1983. The following table summarizes the results:

	New Issues					
	9-7/8% Notes 2/15/86	10-7/8% Notes 2/15/93	10-3/8% Bonds 11/15/07-2012	Total	Maturing Securities Held	Net New Money Raised
Public................	$6.5	$4.5	$3.5	$14.5	$5.8	$8.7
Government Accounts and Federal Reserve Banks...	1.1	0.6	0.4	2.2	2.2	-
Foreign Accounts.....	0.4	(*)	-	0.4	-	0.4
TOTAL................	$8.0	$5.2	$3.9	$17.1	$8.0	$9.2

* $50 million or less.

Details may not add to total due to rounding.

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TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
Friday, February 4, 1983

CONTACT: Charley Powers
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Treasury Announces First Bank Loan Settlement With Iran

Chemical Bank of New York has reached a settlement with Bank Markazi, Iran's Central Bank, and has today received payment on its non-syndicated loan claims against Iran. The payment was made from the escrow account (known as "Dollar Account No. 2") established at the Bank of England with the deposit of $1.418 billion in January 1981, following the release of the U.S. nationals held hostage in Iran. From the amount that was paid out of Dollar Account No. 2, Chemical paid an agreed-upon amount to Markazi in settlement of Iran's claims for interest on blocked Iranian deposits held by Chemical.

This is the first settlement reached by a U.S. bank having outstanding loan claims against Dollar Account No. 2. Other U.S. banks are scheduled to meet in London over the next several months to negotiate their respective claims with Bank Markazi. Additional bank settlements are expected to follow.

John M. Walker, Jr., Assistant Secretary of the Treasury for Enforcement and Operations said, "This is a significant milestone in the implementation of the Algier Accords and in the Iran claims settlement process. After two years of negotiations, U.S. banks are now receiving amounts owed to them by Iran. As banks settle these claims, the claims will be withdrawn from the Iran-United States Claim Tribunal and the burden on the Tribunal, which must still deal with numerous non-bank claims, will be eased considerably."

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R-2019

'REASURY NEWS
nrtment of the Treasury • Washington, D.C. • Telephone 566-2041

FOR USE UPON REQUEST
Monday, February 7, 1983

CONTACT: Marlin Fitzwater
202/566-5252

STATEMENT BY R.T. MCNAMAR
DEPUTY SECRETARY OF THE TREASURY

Monday, February 7, 1983

Neither the State Department, Treasury, the Federal Reserve, the National Security Council, nor the White House Office of Policy Development has had any "preliminary" discussions about suggestions to create a new international agency in the IMF as reported in the Wall Street Journal today. The plan reportedly would have Western governments buy up international bank loans and replace them with long-term negotiable government notes. There is no "high-level Administration task force" considering replacing existing international bank debt with government loans.

The Administration's focus is on securing an accelerated new quota agreement and modifications of the General Arrangements to Borrow for the IMF to ensure it has adequate resources to handle the challenges it faces. While the Reagan Administration continually monitors the international financial, trade, and energy situation, there has been no senior level proposal along the lines contained in the Wall Street Journal article.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

For Immediate Release
Monday, February 7, 1983

Contact: Charles Powers
(202) 566-5252

TAX STATUS OF NEW FARM PROGRAM

The Treasury Department announced today that it will support legislation to avoid any adverse tax consequences to farmers who participate in the Payment in Kind (PIK) program. This legislation will treat farmers who receive commodities for diverting acreage from agricultural use under the PIK program as if they had grown the commodities themselves. Under current law, the farmer would realize gross income in the amount of the fair market value of the commodities received under the PIK program at the time they are made available to the farmer. The farmer would take a tax basis in the commodities equal to the amount included in income.

Under the legislation, which the Administration supports, the commodities received by the farmer will be excluded from gross income and will have a zero basis for income tax purposes. Thus, the farmer will realize income only at the time he sells the commodities. Further, for purposes of the special farm estate tax valuation rules, the farmer will be treated as if he had actually produced the commodities on the acreage diverted from agricultural use under the PIK program.

Agriculture Department officials said the legislation is needed for an effective PIK program. The deadline for farmers to sign up for the program is March 11. Congress will be asked to act quickly on the legislation so that farmers are aware of the tax status prior to the sign-up deadline.

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FOR IMMEDIATE RELEASE
Monday, February 7, 1983

CONTACT: Leon Levine
202/634-2179

TREASURY TO HOLD PAPERWORK REDUCTION CONFERENCE

A conference on reducing the paperwork burden imposed on the public by the Treasury Department and its bureaus was today announced by Cora P. Beebe, Assistant Secretary of the Treasury for Administration.

The conference will be held on Thursday, March 17, 1983, at 10:00 a.m. in the Cash Room of the U.S. Treasury Department located at 15th St., and Pennsylvania Ave., N.W., Washington, D.C.

Assistant Secretary Beebe, who has been designated by the Secretary of the Treasury to carry out departmental responsibiities under the Paperwork Reduction Act of 1980, said that "a major purpose of the conference is to solicit paperwork burden reduction ideas and suggestions from business, trade, professional and consumer groups."

Beebe urged representatives of these groups to "take the opportunity to broaden the Treasury-private sector dialogue begun so successfully at the first departmental paperwork burden conference held on Dec. 2, 1982. The positive response from the private sector to the first meeting," she added, "encouraged the Treasury to convene a second conference and to hold a series of public hearings on paperwork burden around the country later in the year."

Beebe said that the Internal Revenue Service, Bureau of Alcohol, Tobacco and Firearms, Customs Service and other Treasury Bureaus will also report on their current and planned efforts to reduce paperwork.

Requests to speak and written proposals should be submitted by March 9, 1983, to U.S. Treasury Department, Office of Management and Organization, 15th St. and Pennsylvania Ave., N.W., Washington, D.C. 20220, Attention: Paperwork Reduction Conference. Persons who wish to speak should submit outlines of their remarks. Additional information may be obtained by writing to the above address or by calling (202)634-2179.

TREASURY NEWS

epartment of the Treasury • Washington, D.C. • Telephone 566-2041

REMARKS BY
DEPUTY SECRETARY MCNAMAR
BEFORE THE
NATIONAL SAVINGS AND LOAN LEAGUE
MONDAY, FEBRUARY 7, 1983

Your institution's play a significant role in the progress of our economy and the nation. Since your inception, you have worked tirelessly to provide a framework for individual savings and investment.

As the economic recovery continues your role becomes increasingly more important. Greater consumer spending will lead us out of recession. And yours is the institution where people go to save and where capital is available for people to buy a house or a car -- and sales at both are up. I'm sure you welcome this news just as much as we do.

Thomas Jefferson once said "Responsibility is a tremendous engine in a free government." Well this is as true now as it was in 1791 when Jefferson delivered that message to Congress.

This Administration understands and accepts responsibility. It also understands that with responsibility comes the expectation of change and progress.

This is what I want to talk with you about today. The change and progress we has made in implementing a program to permanently strengthen our economy.

The Economy

The development of a sound fiscal and monetary policy was the central objective of the Reagan Administration when it came to office two years ago. For too long a time, Americans had watched the share of GNP accounted for by Federal spending and taxes move upward. As the government siphoned off resources from the private sector and the money supply expanded, economic activity stagnated and inflation soared.

In February 1980 the Administration put before congress a four point plan to revitalize the economy. Our program mandated that:

First, irresponsible and inflationary spending habits were to be stopped.

Second, excessive taxing which had suffocated incentive and productivity was to be cut.

R-2022

Third, the irregular monetary habits of the past were to be replaced by consistent noninflationary practices.

And fourth, the regulatory morass which chained the productive capacities of the private sector was to be cut and disposed of.

The plan called for progress -- progress born through change.

During 1981 and 1982 we implemented major portions of this plan.

The task now is to encourage the renewal of economic growth to reduce unemployment and provide productive job opportunities in the private sector. In so doing we must not repeat the errors of the past and return to an inflationary economy.

The current domestic situation is complicated by the existence of unacceptably large Federal budget deficits and the threat of even larger ones in years to come. These budget deficits will have to be reduced, since their persistence would inevitably lead to very adverse consequences for the U.S. economy and its financial markets. And if fear of failure to reduce the deficits will result in a rekindling of inflationary expectations and higher interest rates.

Many of the economic difficulties we face at home are also faced by countries abroad. The entire international economy is experiencing a severe slowdown, complicated by the special debt-servicing problems of a number of countries. My discussion today deals primarily with the U.S. domestic economy, but it is obvious that the domestic and international situations are closely linked.

It is important to recognize that current difficulties are the culmination of a long period of deteriorating economic performance in this country. It follows that our policies must aim at lasting long-run solutions. There are no quick cures.

The President noted in his State of the Union Address to Congress, "The problems we inherited were far worse than most inside and out of Government had expected; the recession was deeper than most inside and out of Government had predicted. Curing those problems has taken more time, and a higher toll than any of us wanted."

Approach of Administration

The Administration's primary goals of economic recovery have not changed. The fundamental restructuring of the economy still includes:

- bringing inflation under control;

- shifting the composition of activity away from government spending toward more productive endeavors in the private sector;

- providing an environment which would reward innovation, work effort, saving and investment, and in which free-market forces could operate effectively.

Current State of the Economy

The economy now stands poised for recovery. In fact, the recovery may well already be underway at this moment. It has been much longer in coming than we, or for that matter nearly all forecasters, had expected.

The delay in recovery occurred primarily because of the persistence of high interest rates and developments in the international sphere. On the international front, the economies of our leading trading partners continued to weaken. This had an adverse impact on economic activity here. These forces, combined with a general hesitancy on the part of the consumer, led to another round of inventory cutting in the second half of 1982 and delayed the expected turnaround of the economy.

There are now clear signals that the economy is turning around and that the recession will soon be behind us. Encouraging signs include:

- The index of leading indicators has risen for eight out of the last nine months.

- Housing is in the midst of a rapid recovery.

- Business trimmed inventories sharply in the final quarter of last year. Historically, a cleanout of inventories typically has been followed by a shift back to higher rates of production.

- Durable goods spending

- Retail sales have begun to climb.

- Total industrial production stabilized in December and appears poised to turn upward.

- The index of average hourly earnings of production workers in the private nonfarm economy rose at a 5.1 percent annual rate in January from 6 months earlier and was up 5.4 percent from 12 months earlier.

- The unemployment rate fell to 10.4 percent (representing 11.4 million workers) in January from 10.8 percent (12 million) in December.

Policies for the Recovery

In setting policy for the remainder of the 1980's, we must recognize what we must not do. We no longer have the freedom of action to revert back to the overly stimulative monetary and fiscal policies pursued at times in the past, for these would surely lead to a resurgence of inflationary pressures and a new round of rising interest rates. Further, we must not reverse the fundamental tax restructuring put in place in 1981, for this was designed to provide the noninflationary incentives without which the private sector would continue to wither.

Fiscal Year 1984 Budget

The President's Fiscal Year 1984 Budget contains these objectives. It carries a stern message that spending and deficits must be reduced.

The President, as he outlined in his address to Congress, proposed his budget based on four principles. I quote:

"It must be bipartisan. Conquering the deficits and putting the Government's house in order will require the best efforts of all of us.

"It must be fair. Just as all will share in the benefits that will come from recovery, all should share fairly in the burden of transition.

"It must be prudent. The strength of our national defense must be restored so that we can pursue prosperity in peace and freedom while maintaining our commitment to the truly needy.

"Finally, it must be realistic. We cannot rely on hope alone."

The fiscal 1984 budget of $848.5 billion is based on four avenues for deficit reduction. First, a comprehensive Federal spending freeze which will allow 1984 outlays to grow at the predicted rate of inflation. Second, a restructuring of programs in health care, federal retirement and welfare. Third, a reduction in defense spending of $55 billion over the next 5 years. Fourth, a standby deficit reduction program of tax increases to become effective in FY 1986 if -- the economy is not in recession, the proposed freezes have been enacted, and the deficit is greater than 2.5 percent of GNP.

We are projecting receipts for the current year (fiscal year 1983) of $597.5 billion. For fiscal year 1984 we expect receipts to be $659.7 billion. The 1983 figure represents a decline of $20.3 billion from the fiscal year 1982 total of $617.8 billion. This decline, and indeed the absence of an increase in receipts in the range of $50-$70 billion, is explained in large part by the recession.

As I have already explained, our economic projections throughout the remainder of the recovery period are cautious. If real GNP grows at a faster rate than we have projected, then receipts for the current fiscal year as well as for subsequent years will be somewhat higher than we are now projecting.

In 1984, when the recovery will be underway, receipts are expected to rise to $659.7 billion, an increase over 1983 of $62.2 billion, representing an annual growth of 10.4 percent. This will occur as profit margins recover and other income shares continue to grow.

For the other years in our forecast period (1985-1988) we project an average annual growth in receipts of about 10 percent, without contingency taxes (and 11 percent per year including contingency taxes).

All of these projections assume the legislative proposals included in the President's Fiscal Year 1984 Budget are enacted. Receipts under existing legislation will also grow, but at a somewhat lower 9-1/2 percent annual average rate.

It is noteworthy that individual income tax receipts will continue to rise over the 1985-1988 period, but only as <u>real</u> income rises. Beginning in 1985, we will no longer collect hidden taxes in the form of bracket creep caused by inflation. Without the indexation provision of ERTA, individuals would pay $6 billion more in taxes during fiscal year 1985 alone, and about $100 billion more through 1988.

All of these efforts are designed to reduce deficits from nearly 7 percent of GNP today to 2.4 percent by 1988, putting the budget on a path consistent with sustained economic recovery.

<u>Deficits</u>

Spending reductions are really the key to the President's program.

Spending cuts will contribute to the recovery, and the recovery will contribute to deficit reduction. The deficit will fall as the economy advances, particularly if the recovery is a vigorous one. A strong recovery with 1-1/3 percent more real growth per year than in our forecast would bring the budget to near balance by 1988, provided we also curb the growth of Federal outlays.

However, if we fail to bring spending under control and if recovery is slow, we will face a deficit problem which is larger and longer-lasting than we can afford. In such case, the deficit could run in the range of 6 to 7 percent of GNP each year through 1988. Our tax cuts in 1981 were designed to raise the private savings pool. But still we would face the possibility of draining off a large part of the pool of savings, if deficits remain high over the next several years. Interest rates would remain high, and the recovery could stall.

Preferably, all of the necessary narrowing of the deficit would come from the outlay side. Total Federal spending represents the amount of resources absorbed by the government at the expense of the private sector. This spending can be financed by both taxes and borrowing, which in either case amounts to a drain on private resources. Only through spending reduction will the credit market find itself in a more favorable position.

This Administration is determined that deficits of such magnitudes will not come to pass. We came to office with a program of boosting the rate of capital investment in order to place the economy on a faster growth track, and we will not allow ourselves to be diverted from that goal. We will take whatever measures are necessary to narrow the deficit to more acceptable levels, which is at least 2 1/2 percent by 1988.

The President proposes a contingency tax plan to raise revenues of about 1 percent of GNP in the event that after Congress has adopted his spending reduction proposals, there is insufficient economic growth to reduce the deficit below this 2-1/2 percent levels the economy is out of recession, and the proposed freezes on spending have been enacted.

The contingency tax plan would contain two elements, each raising about half of the revenues that may be required.

One would be a temporary surcharge of 5 percent on individuals and corporations. The other element would be a temporary excise tax on domestically produced and imported oil designed to raise revenues of about $5 per barrel. This plan would raise about $146 billion over the 36-month period beginning October 1, 1985.

It is essential to remember that the contingency tax plan is only an insurance plan -- an insurance plan similar to what we all have. For instance, while we don't expect our house to burn down we still buy insurance in the event that it does.

Indexing

Let me touch on two other important considerations related to the budget: repeal of the third year of the tax cuts and indexing.

The 1983 tax cut and tax indexing will be needed to offset bracket creep and of 10 percent on July 1 the increases in social security taxes scheduled to take effect in the future. These measures will greatly improve the competitive standing of American capital and labor in the world as economic recovery proceeds.

Those who would repeal indexing and the 10 percent tax cut due on July 1, 1983, inflict a painful injustice on the working men and women of this country. In 1985, repeal of both of these would mean a 24.3 percent tax increase for those earning less than $10,000 and only a 3.1 percent tax increase for those earning more than $200,000. Seventy-four percent of the benefits of the third year tax cut and indexing go to taxpayers with incomes below $50,000. As a total, repeal would result in a massive $273.2 bilion tax increase between fiscal 1983 and 1988.

Under the full three-year income tax cut plus indexing, the taxpayer would experience by 1984 a decrease in average marginal tax rate to just a shade below those of 1979. The second and third years of the tax cut offset the bracket creep of 1980-1984. Without indexing, however, even the third year of the tax cut fails to provide permanent tax relief. Inflation and bracket creep would repeal the third year of the tax cut by 1985 and the entire tax cut (measured against 1980 tax rates) by 1987. All improvement in incentives would be lost.

As the President has said, it makes no sense to raise taxes just as we are coming out of recession. Nor does it make any sense to so unfairly place the tax burden on the backs of low and middle income families. We need more economic growth in this country that will put people back to work and increase our tax base. Repeal is a bad idea at the wrong time and place.

We are confident that our economic program is the right one for the economy at this critical juncture. The most important signals we can send the economy are spending restraint, deficit restraint, and a commitment to non-inflationary economic growth throughout the decade. This is the program we have devised. Together with the Congress, we can make it work.

I now want to say a few words about the United States role in the world economy.

The major strains in the international financial system which emerged in 1982 had their roots in the rising inflationary pressures in the late 1960's, the twin oil shocks of the 1970's and policy responses that avoided adjustment to new economic realities. Many governments sought to maintain real incomes and employment in uncompetitive industries by subsidies rather than pursue policies to counter inflationary pressures and reallocate resources to reflect new competitive conditions. The results of these policies were higher inflation, slower real economic growth, and large balance of payments deficits an external financing requirements.

The bulk of the external financing was provided through private markets, largely commercial banks, and was heavily concentrated on the developing countries. During 1982, however, financial markets began to recognize that the inflationary environment of the 1970's was changing and that inflationary expectations were undergoing a dramatic shift. Therefore, levels of debt which had previously been considered manageable are now viewed as high in real terms and large in the face of weak export prices and slow world economic growth.

The nature of these difficulties has been known for some time. However, with our own country just beginning to come out of a recession, there is a very natural tendency to feel that the debts of other countries are their debts and not ours.

Because of the pivotal role international trade plays in the U.S. economy this attitude is unrealistic. For instance, this year, if we were to pull back sharply in the absence of any interest or action on the part of the major industrial countries, new lending could begin to dry up. Trade would consequently have to be reduced to match the new lower level of external financing. For the United States, growth would be about 1 percentage point less than we're expecting, and our trade deficit would grow very rapidly due to the loss of $12 billion or so in exports to the developing world. Lost jobs in vital export sectors would compound our recovery efforts.

Assisting nations, including the United States, to make essential financial adjustment is part of the role of the International Monetary Fund. The IMF was founded to promote a sound financial framework for the world economy and is at the center of international efforts to deal with current economic problems.

The IMF is a revolving fund to which each member is obligated to provide its currency to the IMF to finance drawings by other countries facing balance of payments needs; each country in turn has a right to draw upon the IMF in case of balance of payments need.

The re-emergence of large balance of payments financing needs and growing debt problems has led to a sharp resurgence in requests for IMF financing.

Based on a U.S. initiative, agreement has been reached in principle by the major industrialized nations to establish a contingency borrowing arrangement which could be used to deal with threats to the stability of the system. The existing General Arrangement to Borrow (GAB) in the IMF is being increased to about (the equivalent of) $19 billion. In addition we are also negotiating an increase in IMF quotas in the range of 40-50% which would bring the total quotas up to about the (equivalent of) $93 to $100 billion. The U.S. share of the increase, for both the GAB and quotas, would be $7.5 - $8.0 billion.

The initiatives will be further debated and decided on at the February 10th and 11th Interim Committee meeting in

Washington, D.C. At this meeting, the United States will take a lead role in developing solutions for the IMF to deal with the short-term and long-term international financial problems.

The soundness and prosperity of each of the national economies is inextricably linked. It is not possible to get growth at home unless we have a sound world economy. In achieving this goal we will need your help and the assistance of all financial institutions in the country.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE February 7, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $6,003 million of 13-week bills and for $6,003 million of 26-week bills, both to be issued on February 10, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing May 12, 1983			:	26-week bills maturing August 11, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	97.928	8.197%	8.49%	:	95.793	8.322%	8.81%
Low	97.908	8.276%	8.57%	:	95.776	8.355%	8.84%
Average	97.914	8.252%	8.55%	:	95.781	8.345% 2/	8.83%

Tenders at the low price for the 13-week bills were allotted 67%.
Tenders at the low price for the 26-week bills were allotted 90%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 46,605	$ 46,605	:	$ 65,230	$ 28,780
New York	10,359,255	4,633,805	:	13,348,730	5,029,285
Philadelphia	31,830	31,830	:	20,510	19,510
Cleveland	77,445	52,445	:	48,665	23,665
Richmond	62,800	51,800	:	92,955	42,455
Atlanta	53,805	53,805	:	53,425	33,125
Chicago	1,029,240	529,480	:	908,585	258,585
St. Louis	54,825	45,325	:	42,240	35,240
Minneapolis	40,245	28,925	:	40,235	10,735
Kansas City	49,810	49,610	:	39,460	39,430
Dallas	25,995	25,995	:	19,585	14,585
San Francisco	637,570	203,570	:	798,580	205,580
Treasury	249,650	249,650	:	262,165	262,165
TOTALS	$12,719,075	$ 6,002,845	:	$15,740,365	$6,003,140
Type					
Competitive	$10,515,060	$3,798,830	:	$13,409,520	$3,672,295
Noncompetitive	976,090	976,090	:	728,145	728,145
Subtotal, Public	$11,491,150	$4,774,920	:	$14,137,665	$4,400,440
Federal Reserve	1,030,025	1,030,025	:	1,000,000	1,000,000
Foreign Official Institutions	197,900	197,900	:	602,700	602,700
TOTALS	$12,719,075	$6,002,845	:	$15,740,365	$6,003,140

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 8.110%.

R-2023

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

EMBARGOED FOR RELEASE
AFTER 3:30 P.M.
Tuesday, February 8, 1983

CONTACT: Marlin Fitzwater
(202) 566-5252

REMARKS BY
DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE CREDIT UNION NATIONAL ASSOCIATION
FEBRUARY 8, 1983

It's a special pleasure to be with you here this morning for several reasons. To begin with, I had the opportunity last January to speak with many of you at the National Association of Federal Credit Unions annual meeting. At that time, the Administration had a lot of far-reaching plans for deregulating the financial services industry. That was just twelve months ago, and as you all know, since that time major progress has been made in getting the regulatory burden permanently off your backs.

Another reason I've looked forward to this event is that it's not a budget hearing. That is not to say I don't like going up on Capitol Hill to discuss the goals of the Administration. I actually enjoy it very much. I also enjoy going to the dentist and banging into walls! I've spent about 15 hours answering Congressional questions so my forebearance is running almost as thin as my jokes.

For instance, at a recent hearing the room was packed with lobbyists, congressional aides, spectators and the media. There were also quite a few Congressmen. The noise level was high, so before my testimony began, I asked the Congressmen if they could hear me. Immediately a Congressman in the back stood up and shouted "no". With that a Member in the front jumped to his feet, turned to his colleague and said, "Please take my place, I've already heard his opening remarks."

It really is a pleasure to be here today among members of a financial industry that has achieved so much during the last 75 years. Your success is nothing to be taken lightly. After spending thirty-five years on Wall Street, I know what it takes to survive in this industry.

In an environment where survival of the most resourceful dictates, your progress has been outstanding.

Since the first credit union was founded in New Hampshire in 1909, your industry has grown to more than 21,000 credit unions nationwide. From the first deposit of ten cents, your industry now has over $75 billion in total assets. You service more than

43 million people, meaning that today nearly one person in five is a member of a U.S. credit union.

Yet of even greater significance is that your industry is based on a simple idea: the idea that people working together and pooling their savings can create a resource that is otherwise not available to them.

Yours is a story of progress. And this is the theme I want to touch on today regarding the financial industry and the economy.

When President Reagan came to Washington with a plan to limit the size and authority of the government, the pundits had already arrived. With pencils and wit sharpened, they told the President that his plan was for dreamers.

They likened the task of harnessing the federal beast to Ahab's slaying of the great white whale. And they predicted for the President a similar fate.

However, this Administration came to Washington with a mandate from the people, not the pundits. We put together a total economic program, with deregulation as a major component. And it was based on tenets unheard of in the last 50 years.

First, irresponsible and inflationary spending habits were to be stopped.

Second, excessive taxing which had suffocated incentive and productivity was to be cut.

Third, the irregular monetary habits of the past were to be replaced by consistent non-inflationary practices.

And fourth, the regulatory morass which chained the productive capacities of the private sector was to be cut and disposed of.

The plan called for progress -- progress born through change. And nowhere was change and progress more necessary than in the financial industry.

As this audience knows, one of the basic laws governing the financial industry, the Glass Steagall Act, was rolled out of Congress at the same time Henry Ford revolutionized the auto industry with the Model A. Both were great accomplishments. But today we wouldn't expect a Model A to compete at Indy. Likewise we shouldn't expect the laws of the 20's to regulate the financial industry.

The auto industry has come a long way since the Model A. It's a rich history of progress and growth. Well, the banking industry has also come a long way, but we're only halfway to where we should be.

We realize this now. But before we decide where and how fast we should go to make up for lost time, we need to understand how we got here.

After the money-runs and bank failures of the 1930's, the revelation of unrestrained and speculative banking practices led to the need for major reform.

In Congress the banking industry was labeled as more "dangerous than a standing army." And in the streets, bankers were commonly referred to "as a seething den of vipers."

Franklin Delano Roosevelt typified the popular sentiment of the period by saying, "Control is necessary. For every man has a right to his own property; which means a right to be assured, to the fullest extent attainable, of the safety of his savings."

The climate demanded change. And the national mood called for financial control and security which was embodied in the Glass-Steagall Act, the Banking Act of 1935, the Securities Acts of 1933 and 1934, and amendments to the Federal Reserve Act.

These laws were far-reaching in their restructuring of the banking system. They created a new homogeneity among banks and the nation. Where banks were once considered the villians of society, they soon became the foundation for industrial and business recovery.

Banking was now safer and sounder with less financial risk. Regulation had created rock-solid confidence in the industry. As a result, people in the 60s, and 70s became more concerned with convenience, services, and interest rates than the financial health of the institution.

During this period our business and industrial sector underwent explosive growth and change. And in an inflationary economy, investors looked for new ways to make their money work and their assets grow. Consequently, aided by computers, telecommunications and minimal regulation, new non-bank saving alternatives worked their way into the system. Money market mutual funds quickly become a top-shelf investment choice. And while banks and credit unions stood by helplessly restrained, their non-bank competitors gathered in billions of dollars from individual savers.

My point is that while financial markets were radically changing, the regulatory regimen imposed on some segments of the financial industry allowed them to change hardly at all. The first legislation to free such institutions was the Depository Institutions Deregulation and Monetary Control Act of 1980.

Then came passage of the Garn-St Germain Depository

Institution Act of 1982, supported heartily by this Administration, which chipped away some more of the regulatory wall blocking the ability of depository institutions, especially thrift institutions, to compete in the financial services industry.

This bill expands the service powers of thrift institutions, gives the Federal insurance agencies greater flexibility in dealing with emergency mergers and acquisitions, and provides a capital assistance program to support troubled thrift institutions.

It gives credit unions authority to invest in state and local government obligations, and makes numerous other changes providing greater operating flexibility for federal credit unions.

But before the Garn-St Germain Act got its commission to fly, the Depository Institutions Deregulation Committee (DIDC) was in the air battling the forces of regulation.

Since I have been Chairman of the Committee the DIDC has:

-- adopted a schedule to phase out interest rate ceilings on deposits in federally insured commercial banks, savings and loan associations and mutual savings banks;

-- lifted the cap on the 2-1/2 year small savers certificates;

-- developed a new IRA and Keogh account with no federally set interest rate ceiling, and;

-- authorized two short-term deposit instruments.

The DIDC's most recent action has been implementing the landmark New Money Market Deposit Accounts and more recently the Super NOW Accounts. More than $213 billion flowed into the first of these accounts in the first few weeks of its existence, the greatest change in savings habits the country has ever seen. And the Super NOWs have attracted an additional $17 billion. Thrift institutions and savings can now battle with the best and the biggest.

Because the credit union movement is based on the philosophy of service, you've set an example for the entire thrift industry. You've been aggressive in offering the new investment instruments. And consequently, you have been very competitive in the market.

Under the leadership of Chairman Callahan, you've carried some water for the entire deregulatory movement. And we at the Treasury notice and appreciate that contribution. Significant gains have been made in deregulating interest rates. Yet this is only the beginning in restoring health to the industry.

So far we've only replaced some parts of the financial machine. But this industry is like a locomotive -- and all the parts must work together smoothly and efficiently for it to run at full power. We still need an overall framework for the management and administration of the new powers in Garn-St Germain, and those yet to come.

Right now, the law is being reshaped in an uncertain case-by-case basis. And like using gum to stop the leak in a pipe, something's bound to burst. Not only do the financial industries differ as to what is legal and rightfully theirs, but the regulatory agencies can't agree on what is permissible competition.

As you know, last year the Administration sent a proposal to the 97th Congress which would have allowed bank holding companies through subsidiaries to offer a broad range of services. The legislation sought to enhance the competitive ability of traditional depository institutions. Although it was not voted on in the 97th Congress, with industry support -- it's designed to help <u>them</u> -- we plan to reintroduce the legislation this year.

At the same time, we all recognize the importance of keeping soundness in the financial services industry. So the goal of that legislation is to define a system in which financial institutions can take banking risks and other financial or commercial risks, but through bank holding companies. Thus, a broader range of services can be offered while insuring the soundness of the system.

Getting this kind of legislation passed into law will not be easy. We'll need your help and the support of the entire financial industry.

Deregulation has one other dimension that I want to mention in closing.

Cutting unnecessary regulation is like pulling up old roots. Even though the root looks dead, it is sometimes very difficult to extract. And typically when it's finally pulled out, you discover it's five times longer than you thought it would be.

Well, this has been the problem with pruning the financial regulatory system. There are just a lot more regulations than we originally expected. We've pulled out a lot of roots, but they're only surface roots. So, in order to bring health to the system, we've got to go deeper and continue extracting and pruning.

Over the past half century, the Federal government has developed an overly complex apparatus for regulating our financial institutions. For example, the commercial banking industry alone is subject to three separate Federal regulatory agencies. We also have three separate agencies providing deposit insurance for depository institutions. The result has been duplication, overlapping of duties, and fragmented authority.

After years of regulatory inefficiency, we need to seriously examine proposals for streamlining the apparatus. That's exactly what we're doing in the Vice President's Task Group on Regulation of Financial Services; he chairs the group, and I am the Vice-Chairman.

The Task Group has several major goals. First, we want to insure that Federal regulation of different kinds of financial institutions is consistent and equitable: no category of institutions should enjoy any kind of preferential treatment just because it happens to be subject to one regulatory agency rather than another. Second, we want to insure coherent and effective Federal responses to certain policy problems which now tend to get entangled in the conflicting or overlapping jurisdictions of the various agencies. I am thinking, for example, of the regulation of bank holding companies, and the handling of failing institutions. Finally, we want to see what we can do to reduce the burdens on financial institutions of redundant or unnecessary reporting requirements and other regulations which are associated with the existing organizational structure.

On January 11 this task force -- and Chairman Callahan is a member -- held its first meeting. The results were encouraging. We set ourselves a timetable of nine months to examine all aspects of the problem and to produce specific legislative proposals.

Doing all of that in nine months in quite a challenge. But it's a task long overdue, and we've got strong support in the agencies and from the heads of all the depository institution regulators.

Deregulation and reform is no longer a dream of the future. It is a reality of the present. The response to unlimited interest rate accounts and thrift institution money market accounts is proof that the public wants more from its financial institutions.

The Administration's commitment to deregulation embraces this public demand. And as we develop legislation to meet the expanded needs of the country, we will be guided by one major principle: the best interests of the consumer.

Perhaps that phrase, "the best interests of the consumer," is a good place to mention withholding of taxes on dividends and interest. I realize that the Credit Union National Association is urging repeal of this important tax compliance measure. I also realize that at least one Administration official has suggested that we might change our position on this issue. Well he's wrong.

The Administration remains committed to the withholding of dividend and interest income. And I am frankly appalled that some financial institutions have used questionable scare tactics to suggest that this is a new tax, or that retired people will lose their savings, or that banks will lose their shirts in performing this function.

My response is: You won't lose your shirts unless you lose your heads.

One notice reached new heights of demagoguery by saying that old people would lose -- and I quote -- "money that might otherwise go to pay for food, housing and medical bills." Someone should be ashamed. There are no new taxes involved and over 85 percent of retired people are exempt.

Another bank ad suggests that to get an exemption you have to reveal your financial condition. Nonsense. You need only declare whether or not your taxes are above or below a certain level. Both you, the bank and the IRS already know far more than that about your customers.

Another ad suggests that bankers don't want to be tax collectors. Nonsense. They already withhold taxes on employee wages. And so does every other company in America. Even distillers and tobacco companies collect taxes and still make a profit.

Another ad says the exemption form is too hard to fill out. Nonsense. It requires a name, address, social security number and a check mark in the exemption box. It's no more difficult than filling out a deposit slip.

Indeed, we let the banks design their own exemption form so they can make it as easy as they want.

And finally, if we do lose withholding we would have to make up the $26 billion in tax revenues we would collect through 1988 with some new tax that really would affect consumers or business.

In any case, financial institutions and the government have a lot of important issues to deal with in the next few months -- issues that will improve your profits and your ability to compete. It's time we focused on these issues and got on with the important business of deregulation.

Thank you.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

Remarks by
The Honorable Roy G. Hale
Treasurer of the United States (Acting)

First Striking of the Olympic Coin
at the San Francisco Mint
February 10, 1983

Good morning everyone. And thank you, Donna, for that kind introduction. It is my pleasure to be here to represent Angela M. Buchanan, the Treasurer of the United States, and say a few words on behalf of the Olympic Coin Program.

We are particularly pleased to have such a large turnout for this exciting moment. Today, as you know, we are gathered here to strike the first of three precious metal coins to benefit the United States Olympic movement and amateur sports in this country. Striking this 1983 silver coin represents a significant step in an honorable effort that began some 20 months ago when Congressman Frank Annunzio, Chairman of the House Subcommittee on Consumer Affairs and Coinage, sponsored this country's first Olympic Coin bill. The overall goal of this legislation is to provide financial support for competitive amateur sports.

The legislation is thoughtfully written and designed so that -- by establishing a surcharge on each coin sold -- funds will be provided for the Olympic Program at no cost to the United States Government or to the American taxpayer. Fifty percent of the surcharges are earmarked for the United States Olympic Committee to train United States athletes, to support local or community amateur athletic programs and to erect facilities for the training of such athletes. The remaining 50 percent surcharge will go to the Los Angeles Olympic Organizing Committee to stage and promote the 1984 games in Los Angeles, California, July 28 to August 12, 1984.

There has been a rapid chain of events since President Reagan signed into law last July this Nation's first Olympic Commemorative Coin Act:

* October 15 -- three months after the new law was on the books, the Treasury announced the kickoff of the new program. This included the selection of 6 preliminary designs for the obverse and reverse sides of the coins, and the beginning of coin sales.

R-2025

* Forty-five days later -- on November 30 -- Treasury announced gross sales of 630,000 coins for $48 million and the first surcharge check of $10 million for the Olympic committees.

* By December 23, gross sales totaled over $58 million with an additional $3.3 million for surcharges.

* As of January 31, gross sales had climbed to 829,000 coins totalling $62 million. As a result, we have transferred a total of $14.3 million in surcharges to the two Olympic Committees.

Looking ahead to February 28, proposals are due in our office from firms interested in marketing Olympic coins internationally. By April 1 of this year, the marketing program for Olympic coins should be in full swing in this country and around the world.

We are pleased so far with the public's response to our initial offering of Olympic coins. Now, with the striking of the first coin and the beginning of a major marketing program, we are really getting this program moving. Today is truly a momentous occasion for the Olympic movement in this country.

Thank you for coming and in closing I would just like to quote from our nationwide public advertisement this week:

"C'mon America, Invest in Your Team."

Thank you.

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TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

February 8, 1983

FACT SHEET

United States Joins African Development Bank

President Reagan today signed the necessary documentation accepting United States membership in the African Development Bank.

In 1972, non-regional countries joined Bank members in establishing the African Development Fund to provide concessional financing to the poorest African countries. In 1979, the Governors of the Bank extended the offer of membership to the United States and other non-regional countries.

In 1981, Congress authorized both U.S. membership in the African Development Bank and a U.S. subscription of $359.7 million of Bank capital. Also in 1981, the first installment ($17.99 million of paid-in capital and $53.96 million of callable capital) was enacted by the Congress. Four additional installments with identical amounts for paid-in and callable capital subscriptions will be sought in the FY 1984-1987 period.

United States membership in the African Development Bank reflects this country's growing economic and security interests in this important region, and our desire to cooperate in a constructive multilateral effort to help the countries of Africa overcome their very serious development problems.

Background on the African Development Bank

The African Development Bank, with headquarters in Abidjan in the Ivory Coast, was established in 1963, by 30 African countries to make loans on near-market terms to promote economic and social development in member countries individually and through regional cooperation. Under the terms of the original Articles of Agreement, membership was restricted to independent African countries. There are currently 50 African member countries. In 1972, Bank members joined with non-regional countries to establish the African Development Fund to provide financing on concessional terms to the poorest African countries. The United States became a member of the Fund in 1976.

The Bank finances its loan operations primarily from the paid-in capital subscriptions of member countries and funds raised through borrowings or guarantees in international capital markets. Lending operations totaled $1,663 million as of year-end 1981, with lending concentrated in public utilities (32 percent), industry and development banks (25 percent), transport (24 percent) and agriculture (17 percent).

Although Bank resources have increased significantly, the absence of industrial countries severely limited the Bank's access to world capital markets. In May 1979, the Governors of the African Development Bank agreed, subject to the necessary ratification by member governments, to invite non-African countries to join the Bank. Twenty-one non-regional countries subsequently agreed to subscribe a total of $2.1 billion to the Bank, 25 percent in paid-in capital and 75 percent in callable capital. The United States share of the non-regional subscription is 17.04 percent, i.e., $89.93 million in paid-in capital and $269.80 million in callable capital.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M.

February 8, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $12,400 million, to be issued February 17, 1983. This offering will provide $ 1,225 million of new cash for the Treasury, as the maturing bills are outstanding in the amount of $11,169 million, including $ 1,144 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and $ 1,918 million currently held by Federal Reserve Banks for their own account. The two series offered are as follows:

91-day bills (to maturity date) for approximately $6,200 million, representing an additional amount of bills dated May 20, 1982, and to mature May 19, 1983 (CUSIP No. 912794 CC 6), currently outstanding in the amount of $11,212 million, the additional and original bills to be freely interchangeable.

182-day bills for approximately $ 6,200 million, to be dated February 17, 1983, and to mature August 18, 1983 (CUSIP No. 912794 DM 3).

Both series of bills will be issued for cash and in exchange for Treasury bills maturing February 17, 1983. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

R-2026

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, February 14, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on February 17, 1983, in cash or other immediately-available funds or in Treasury bills maturing February 17, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. TREASURY February 9, 1983

TREASURY TO AUCTION $7,500 MILLION OF 2-YEAR NOTES

The Department of the Treasury will auction $7,500 million of 2-year notes to refund $4,939 million of 2-year notes maturing February 28, 1983, and to raise $2,561 million new cash. The $4,939 million of maturing 2-year notes are those held by the public, including $768 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities.

The $7,500 million is being offered to the public, and any amounts tendered by Federal Reserve Banks as agents for foreign and international monetary authorities (including the $768 million of maturing securities) will be added to that amount.

In addition to the public holdings, Government accounts and Federal Reserve Banks, for their own accounts, hold $499 million of the maturing securities that may be refunded by issuing additional amounts of the new notes at the average price of accepted competitive tenders.

Details about the new security are given in the attached highlights of the offering and in the official offering circular.

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Attachment

R-2027

HIGHLIGHTS OF TREASURY
OFFERING TO THE PUBLIC
OF 2-YEAR NOTES
TO BE ISSUED FEBRUARY 28, 1983

February 9, 1983

Amount Offered:

To the public........................$7,500 million

Description of Security:

Term and type of security............2-year notes
Series and CUSIP designation.........Series R-1985
(CUSIP No. 912827 PE 6)
Maturity date........................February 28, 1985
Call date............................No provision
Interest rate........................To be determined based on the average of accepted bids
Investment yield.....................To be determined at auction
Premium or discount..................To be determined after auction
Interest payment dates...............August 31, 1983; February 29, 1984; August 31, 1984; and February 28, 1985
Minimum denomination available.......$5,000

Terms of Sale:

Method of sale.......................Yield Auction
Competitive tenders..................Must be expressed as an annual yield, with two decimals, e.g., 7.10%
Noncompetitive tenders...............Accepted in full at the average price up to $1,000,000
Accrued interest payable by investor.........................None
Payment by non-institutional investors..........................Full payment to be submitted with tender
Deposit guarantee by designated institutions..............Acceptable

Key Dates:

Deadline for receipt of tenders......Wednesday, February 16, 1983, by 1:30 p.m., EST
Settlement date (final payment due from institutions)
a) cash or Federal funds...........Monday, February 28, 1983
b) readily collectible check.......Thursday, February 24, 1983

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 12:00 NOON February 11, 1983

TREASURY'S 52-WEEK BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for approximately $ 7,750 million of 364-day Treasury bills to be dated February 24, 1983, and to mature February 23, 1984 (CUSIP No. 912794 ED 2). This issue will provide about $ 2,475 million new cash for the Treasury, as the maturing 52-week bill was originally issued in the amount of $ 5,271 million.

The bills will be issued for cash and in exchange for Treasury bills maturing February 24, 1983. In addition to the maturing 52-week bills, there are $11,153 million of maturing bills which were originally issued as 13-week and 26-week bills. The disposition of this latter amount will be announced next week. Federal Reserve Banks as agents for foreign and international monetary authorities currently hold $1,648 million, and Federal Reserve Banks for their own account hold $3,026 million of the maturing bills. These amounts represent the combined holdings of such accounts for the three issues of maturing bills. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average price of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them. For purposes of determining such additional amounts, foreign and international monetary authorities are considered to hold $320 million of the original 52-week issue.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. This series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Thursday, February 17, 1983. Form PD 4632-1 should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

R-2028

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders, the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on February 24, 1983, in cash or other immediately-available funds or in Treasury bills maturing February 24, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

FOR IMMEDIATE RELEASE FEBRUARY 14, 1983

The Treasury announced today that the 2-1/2 year Treasury yield curve rate for the five business days ending February 14, 1983, averaged 9.90 % rounded to the nearest five basis points. Ceiling rates based on this rate will be in effect from Tuesday, February 15, 1983 through Monday, February 28, 1983.

Detailed rules as to the use of this rate in establishing the ceiling rates for small saver certificates were published in the Federal Register on July 17, 1981.

Small saver ceiling rates and related information is available from the DIDC on a recorded telephone message. The phone number is (202)566-3734.

Approved________________________________
Francis X. Cavanaugh, Director
Office of Government Finance
& Market Analysis

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

STATEMENT OF THE HONORABLE DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
SENATE COMMITTEE ON BANKING,
HOUSING AND URBAN AFFAIRS
Washington, D.C.
February 14, 1983

IMF Resources, World Financial Stability, and U.S. Interests

Mr. Chairman and members of the Committee:

It is a pleasure to appear before you today to explain and support the Administration's proposals for legislation to increase the resources of the International Monetary Fund.

After extensive consultations and negotiations among IMF members, agreement was completed last Friday on complementary measures to increase IMF resources: an increase in quotas, the IMF's basic source of financing; and an expansion of the IMF's General Arrangements to Borrow (GAB), for lending to the IMF on a contingency basis, if needed to deal with threats to the international monetary system. These must now be confirmed by member governments, involving Congressional authorization and appropriation in our case, in order to become effective. As background to our legislative proposals, which we will submit formally within a very few days, I would like to outline the problems facing the international financial system, the importance to the United States of an orderly resolution of those problems, and the key role the IMF must play in solving them.

R-2029

The International Financial Problem

Since about the middle of last year, the international monetary system has been confronted with serious financial problems. The debt and liquidity problems of Argentina, Brazil, Mexico, and a growing list of other borrowers became front-page news -- and correctly so, since management of these problems is critical to our economic interests. Bluntly stated, the problem is that the debts of many key countries became too large for them to continue to manage under present policies and world economic circumstances; lenders began to retrench sharply; and the borrowers have been finding it difficult if not impossible to scrape together the money to meet upcoming debt payments and to pay for essential imports. As a result, the international financial and economic system is experiencing strains that are without precedent in the postwar era and which threaten to derail world economic recovery.

There is a natural tendency under such circumstance for financial contraction and protectionism -- reactions that were the very seeds of the depression of the 1930s. It was in response to those tendencies that the International Monetary Fund was created in 1944, largely at the initiative of the U.S. government, to offer a backstop and underlying support mechanism to prevent a recurrence of that slide into depression. If the IMF is to be able to continue in that role, it must have adequate resources to deal with the current situation.

The current problem did not arise overnight, but rather stems from the economic environment and policies pursued over the last two decades. Inflationary pressures began mounting during the 1960's, and were aggravated by the commodity boom of the early 1970's and the two oil shocks that followed. For most industrialized countries, the oil shocks led to a surge of imported inflation, worsening the already growing inflationary pressures; to large transfers of real income and wealth to oil exporting countries; and to deterioration of current account balances. For the oil-importing less developed countries -- the LDCs -- this same process was further compounded by their loss of export earnings when the commodity boom ended.

For both industrial and developing countries, the appropriate policy response to all these events would have been a combination of fiscal and monetary restraint to resist inflationary pressure, and willingness to let structural adjustments take place to adapt their economies to the higher relative price of energy. The higher energy price made many industries less competitive, and adjustment required that resources be shifted away from them. Similarly, the transfer of real income and wealth to OPEC implied a reduction in real income at home.

Instead, most governments tried to maintain real incomes through stimulative economic policies, and to protect jobs in uncompetitive industries through controls and subsidies. Inflationary policies did bring a short-run boost to real growth at times, but in the longer run they led to higher inflation, declining investment and productivity, and worsening prospects for real growth and employment.

Similarly, while these policies delayed economic adjustment somewhat, they could not put it off forever. In the meanwhile, the size of the adjustment needed was getting larger. Important regions remained dependent on industries whose competitive position was declining; inflation rates and budget deficits soared; and --

most pertinent to today's financial problems -- many oil importing countries experienced persistent, large current account deficits and unprecedented external borrowing requirements.

In the inflationary environment of the 1970's, it was fairly easy for most nations to borrow abroad, even in such large amounts. Commercial banks were "recycling" surplus OPEC funds; interest rates were low in relation to current and expected inflation; and both borrowers and lenders expected that continued inflation would lead to ever-increasing export revenues and reduce the real burden of foreign debts. As a result, many countries' foreign debts continued to grow too rapidly for too many years.

Most of the increased foreign debt reflected borrowing from commercial banks in industrial countries. By mid-1982, the total foreign debt of non-OPEC developing countries was something over $500 billion -- more than five times the level of 1973. Of that total, roughly $270 billion was owed to commercial banks in the industrial countries, and more than half of that was owed by only three Latin American countries -- Argentina, Brazil, and Mexico. New net lending to non-OPEC LDCs by banks in the industrial countries grew at a rising pace -- about $37 billion in 1979, $43 billion in 1980, and $47 billion in 1981 -- with most of the increase continuing to go to Latin America. (See Charts A and B.)

That there has been inadequate adjustment and excessive borrowing has become painfully clear in the current economic environment -- one of stagnating world trade, disinflation, declining commodity prices, and interest rates which are still high by historical standards. Over the past two years, there has been a strong shift to anti-inflationary policies in most industrial countries, and this shift has had a major impact on market attitudes. Market participants are beginning to recognize that our governments intend to keep inflation under control in the future and are adjusting their behavior accordingly.

In most important respects, the impact of this change has been positive. Falling inflation expectations have led to major declines in interest rates. There has been a significant drop in the cost of imported oil. On the financial side, there is a shift toward greater scrutiny of foreign lending which may be positive for the longer run, even though there are short-term strains. Lenders are re-evaluating loan portfolios established under quite different expectations about future inflation. Levels of debt that were once expected to decline in real terms because of continued inflation -- and therefore to remain easy for borrowers to manage -- are now seen to be high in real terms and not so manageable in a disinflationary world. As a result, banks have become more cautious in their lending -- not just to LDCs but to domestic corporations as well.

There is certainly nothing wrong with greater exercise of prudence and caution on the part of commercial banks -- far from it. Since banks have to live with the consequences of their decisions, sound lending judgment is crucial. In addition, greater scrutiny by lenders puts pressure on borrowers to improve their capacity to repay, and creates an additional incentive for borrowing countries to undertake needed adjustment measures.

But a serious short-run problem has arisen as a result of the size of the debt of several key countries, the turn in the world economic environment, inadequacy of adjustment policies, and the speed with which countries' access to external financing has been cut back. Last year, net new bank lending to oil importing LDCs dropped by roughly half, to something in the range of $20 to $25 billion for the year as a whole (Chart B), and came to a virtual standstill for a time at mid-year. This forced LDCs to try to cut back their trade and current account deficits sharply to match the reduced amount of available external financing.

The question is one of the speed and degree of adjustment. While the developing countries must adjust their economies to reduce the pace of external borrowing and maintain their capacity to service debt, there _is_ a limit, in both economic and political terms, to the speed with which major adjustments can be made. Effective and orderly adjustment takes time, and attempts to push it too rapidly can be destabilizing.

The only fast way for these countries to reduce significantly their deficits in the face of an abrupt cutback in financing is to cut imports drastically, either by sharply depressing their economies to reduce demand or by restricting imports directly. Both of these are damaging to the borrowing countries, politically and socially disruptive, and painful to industrial economies like the United States -- because almost all of the reduction in LDC imports must come at the direct expense of exports from industrial countries. They are exactly the sort of reaction that the IMF was created to avoid. But as the situation has developed in recent months, there has been a danger that lenders might move so far in the direction of caution that they compound the severe adjustment and liquidity problems already faced by major borrowers, and even push other countries which are now in reasonably decent shape into serious financing problems as well.

Importance to the United States of an Orderly Resolution

It is right for American citizens to ask why they and their government need be concerned about the international debt problem. Why should we worry if some foreign borrowers get cut off from bank loans? And why should we worry if banks lose money? Nobody forced them to lend, and they should live with the consequences of their own decisions like any other business.

If all the U.S. government had in mind was throwing money at the borrowers and their lenders, it would be difficult to justify using U.S. funds on any efforts to resolve the debt crisis, especially at a time of domestic spending adjustment.

But of course, there is more to the problem, and to the solution. First, a further abrupt and large-scale contraction of LDC imports would do major damage to the U.S. economy. Second, if the situation were handled badly, the difficulties facing LDC borrowers might come to appear so hopeless that they would be tempted to take desperate steps to try to escape. The present situation is manageable. But a downward spiral of world trade and billions of dollars in simultaneous loan losses would pose a fundamental threat to the international economic system, and to the American economy as well.

In order to appreciate fully the potential impact on the U.S. economy of rapid cutbacks in LDC imports, it is useful to look at how important international trade has become to us. Trade was the fastest growing part of the world economy in the last decade -- but the volume of U.S. exports grew even faster in the last part of the 1970's, more than twice as fast as the volume of total world exports. By 1980, nearly 20 percent of total U.S. production of goods was being exported, up from 9 percent in 1970, although the proportion has fallen slightly since then. (Charts C and D.)

Among the most important export sectors for this country are agriculture, services, high technology, crude materials and fuels. American agriculture is heavily export-oriented: one in three acres of U.S. agricultural land, and 40 percent of agricultural production, go to exports. This is one sector in which we run a consistent trade surplus, a surplus that grew from $1.6 billion in 1970 to over $24 billion in 1980. (Chart E.)

Services trade -- for example, shipping, tourism, earnings on foreign direct investment and lending -- is another big U.S. growth area. The U.S. surplus on services trade grew from $3 billion in 1970 to $34 billion in 1980, and has widened further since. (Chart F.) When both goods and services are combined, it is estimated that one-third of U.S. corporate profits derive from international activities.

High technology manufactured goods are a leading edge of the American economy, and not surprisingly exports of these goods have grown in importance. They rose from $7.6 billion in 1970 to $40 billion in 1980. And even in a sector we do not always think of as dynamic -- crude materials and non-petroleum fuels like coal -- exports rose six-fold, from $2.4 billion to $14.6 billion over the same period.

Vigorous expansion of our export sectors has become critical to employment in the United States. (Chart G.) The absolute importance of exports is large enough -- they accounted directly for 5 million jobs in 1982, including one out of every eight jobs in manufacturing industry. But export-related jobs have been getting even <u>more</u> important at the margin. A survey in the late 1970s indicated that four out of every five <u>new</u> jobs in U.S. manufacturing was coming from foreign trade; on average, it is estimated that every $1 billion increase in our exports results in 24,000 new jobs.

Later I will detail how Mexican debt problems have caused a $10 billion annual-rate drop in our exports to Mexico between the end of 1981 and the end of 1982. By the rule of thumb I just gave, that means the loss of a quarter of a million American jobs.

These figures serve to illustrate the overall importance of exports to the U.S. economy. The story can be taken one step further, to relate it more closely to the present financial situation. Our trading relations with the LDCs have expanded even more rapidly than our overall trade. Our exports to the LDCs, which accounted for about 25 percent of total U.S. exports in 1970, rose to about 29 percent by 1980. (Chart H.) In manufactured goods, which make up two-thirds of our exports, the share going to LDCs rose even more strongly -- from 29 percent to 39 percent. In fact, since the mid-1970's trade with LDCs has accounted for more than half of the overall growth of American exports.

What these figures mean is that the export sector of our economy -- a leader in creating new jobs -- is tremendously vulnerable to any sharp cutbacks in imports by the LDCs. Yet that is exactly the response to which debt and liquidity problems have been driving them. This is a matter of concern not just to the banking system, but to American workers, farmers, manufacturers and investors as well.

Even on the banking side, there are indirect impacts of concern to all Americans. A squeeze on earnings and capital positions from losses on foreign loans not only would impair banks' ability to finance world trade, but also could ultimately mushroom into a significant reduction in their ability to lend to domestic customers and an increase in the cost of that lending.

Beyond our obvious interest in maintaining world trade and trade finance, there is another less-recognized U.S. financial interest. The U.S. government faces a potential exposure through Federal lending programs administered by Eximbank and the Commodity Credit Corporation. This exposure -- built in support of U.S. export expansion -- amounted to $35 billion at the end of 1982, including $24 billion of direct credits (mostly from Eximbank) and $11 billion of guarantees and insurance. Argentina, Brazil and Mexico are high on the list of borrowers. Should loans extended or guaranteed under these programs sour, the U.S. Treasury -- meaning the U.S. taxpayer -- would be left with the loss. We have a direct interest in avoiding this addition to Federal financing requirements.

All industrial economies, including the American economy, will inevitably bear some of the costs of the balance of payments adjustments LDCs must make and are already making. This adjustment would be much deeper, for both the borrowing countries and for lending countries like the United States, if banks were to pull back <u>entirely</u> from new lending this year. In 1983, for example, a flat standstill would require borrowers to make yet another $20 to $25 billion cut in their trade and current account deficits, which would be considerably harder to manage if it came right on the heels of similar cuts they have already made. If these countries were somehow to make adjustments of that size for a second consecutive year, the United States and other industrial countries would then have to suffer large export losses once again. At the early stages of U.S. and world economic recovery we are likely to be in this year, a drop in export production of this size could abort the gradual rebuilding of consumer and investor confidence we need for a sustained recovery.

In fact, many borrowers have already taken very difficult adjustment measures to get this far. If they were forced to contemplate a second year of further massive cutbacks in available financing, they could be driven to consider other measures to reduce the burden of their debts. Here potentially lies a still greater threat to the financial system.

When interest payments are more than 90 days late, not only are bank profits reduced by the lost interest income, but they may also have to begin setting aside precautionary reserves to cover potential loan losses. If the situation persisted long enough, the capital of some banks might be reduced.

Banks are required to maintain an adequate ratio between their underlying capital and their assets -- which consist mainly of loans. For some, shrinkage of their capital base would force them to cut back on their assets -- meaning their outstanding loans -- or at least on the growth of their assets -- meaning their new lending. Banks would thus be forced to make fewer loans to all borrowers, domestic and foreign, and they would also be unable to make as many many investments in securities such as municipal bonds. Reduced access to bank financing would not only force a cutback in the expenditures which private corporations and local governments can make -- it would also put upward pressure on interest rates.

The usual perception of international lending is that it involves only a few large banks in the big cities, concentrated in half a dozen states. The facts are quite different. We have reliable information from bank regulatory agencies and Treasury reports identifying nearly 400 banks in 35 states and Puerto Rico that have foreign lending exposures of over $10 million --

and in all likelihood there are hundreds more banks with exposures below that threshhold but still big enough to make a significant dent in their capital and their ability to make new loans here at home. Banks in most states are involved, and the more abruptly new lending to troubled borrowing countries is cut back, the more likely it is that the fallout from their problems will feed back back on the U.S. financial system and weaken our economy. Many U.S. corporations also have claims on foreign countries, related to their exports and foreign investments.

Resolving the International Financial Problem

Debt and liquidity problems did not come into being overnight, and a lasting solution will also take some time to put into place. We have been working on a broad-based strategy involving all the key players -- LDC governments, governments in the industrialized countries, commercial banks, and the International Monetary Fund. This strategy has five main parts:

First, and in the long run most important, must be effective adjustment in borrowing countries. In other words, they must take steps to get their economies back on a stable course, and to make sure that imports do not grow faster than their ability to pay for them. Each of these countries is in a different situation, and each faces its own unique constraints. But in general, orderly and effective adjustment will not come overnight. The adjustment will have to come more slowly, and must involve expansion of productive investment and exports. In many cases it will entail multi-year efforts, usually involving measures to address some combination of the following problems: rigid exchange rates; subsidies and protectionism; distorted prices; inefficient state enterprises; uncontrolled government expenditures and large fiscal deficits; excessive and inflationary money growth; and interest rate controls which discourage private savings and distort investment patterns. The need for such corrective policies is recognized, and being acted on, by major borrowers -- with the support and assistance of the IMF.

The second element in our overall strategy is the continued availability of official balance of payments financing, on a scale sufficient to help see troubled borrowers through the adjustment period. The key institution for this purpose is the International Monetary Fund. The IMF not only provides temporary balance of payments financing, but also ensures that use of its funds is tied tightly to implementation of needed policy measures by borrowers. It is this aspect -- IMF conditionality -- that makes the role of the IMF in resolving the current debt situation and the adequacy of its resources so important.

IMF resources are derived mainly from members' quota subscriptions, supplemented at times by borrowing from official sources. Assessing the adequacy of these resources over any extended period is extremely difficult and subject to wide margins of error. The potential needs for temporary balance of payments financing depend on a number of variables, including members' current and prospective balance of payments positions, the availability of other sources of financing, the strength of the conditionality associated with the use of IMF resources, and members' willingness and ability to implement the conditions of IMF programs. At the same time, the amount of IMF resources that is effectively available to meet its members' needs at any point in time depends not only on the size of quotas and borrowing arrangements, but also on the currency composition of those resources in relation to balance of payments patterns, and on the amount of members' liquid claims on the IMF which might be drawn. In view of all these variables, assessments of the IMF's "liquidity" -- its ability to meet members' requests for drawings -- can change very quickly.

Still, as difficult as it is to judge the adequacy of IMF resources in precise terms, most factors point in the same direction at present. The resources now effectively available to the IMF have fallen to very low levels, both in absolute terms and in relation to actual and potential use of the IMF.

At the beginning of this year, the IMF had about SDR 28 billion available for lending. However, SDR 19 billion of that total had already been committed under existing IMF programs or was expected to be committed shortly to programs already negotiated, leaving only about SDR 9 billion available for new commitments. Given the scope of today's financing problems, requests for IMF programs by many more countries must be anticipated over the next year, and it is probable that the IMF's ability to commit resources to future adjustment programs will be exhausted by late 1983 or early 1984.

It is therefore clear that the Fund's liquidity position will be under extreme strain in the near future. Since actual drawings under its program commitments are phased over time and tied to the borrower's performance of policy conditions, the Fund has sufficient resources to meet its immediate short-run cash needs. But there is no provision for the future, and the margin of safety for the present is very small and shrinking rapidly. The Fund's ability to continue committing resources to adjustment programs, and to permit its current holdings to be drawn down significantly further, depends importantly on assurances that new resources will be provided soon. I will return to our specific proposals in this area shortly.

The IMF cannot be our only buffer in financial emergencies. It takes time for borrowers to design and negotiate lending programs with the IMF and to develop financing arrangements with other creditors. As we have seen in recent cases, the problems of troubled borrowers can sometimes crystallize too quickly for that process to reach its conclusion -- in fact, the real liquidity crunch came in the Mexican and Brazilian cases before such negotiations even started.

Thus, the third element in our strategy is the willingness of governments and central banks in lending countries to act quickly to respond to debt emergencies when they occur. Recent experience has demonstrated the need to consider providing immediate and substantial short-term financing -- on a selective basis, where system-wide dangers are present -- to tide countries through their negotiations with the IMF and discussions with other creditors. We are undertaking this where necessary, on a case-by-case basis, through ad hoc arrangements among finance ministries and central banks, often in cooperation with the Bank for International Settlements. But it must be emphasized that these lending packages are short-term in nature, designed to last for only a year at most and normally much less, and cannot substitute for IMF resources which are designed to help countries through a multi-year adjustment process.

In fact, IMF resources themselves have only a transitional and supporting role. The overall amount of Fund resources, while substantial, is limited and not in any event adequate to finance the needs of its members. While we feel that a sizeable increase in IMF resources is essential, this increase is not a substitute for lending by commercial banks. Private banks have been the largest single source of international financing in the past to both industrial and developing countries, and this will have to be the case in the future as well -- including during the crucial period of adjustment.

Thus, the fourth essential element in resolving debt problems is continued commercial bank lending to countries that are pursuing sound adjustment programs. In the last months of 1982 some banks, both in United States and abroad, sought to limit or reduce outstanding loans to troubled borrowers. But an orderly resolution of the present situation requires not only a willingness by banks to "roll over" or restructure existing debts, but also to increase their net lending to developing countries, including the most troubled borrowers, to support effective, non-disruptive adjustment. The increase in net new commercial bank lending needed for just three countries -- Brazil, Argentina, and Mexico -- will approach $11 billion in 1983. Without this continued lending in support of orderly and constructive economic adjustment, the programs that have been formulated with the IMF cannot succeed -- and the lenders have a strong self-interest in helping to assure success. It should be noted, however, that new bank lending will be at a slower rate than that which has characterized the last few years -- more in line with the increase in 1982 than what we saw in 1980 or 1981.

The final part of our strategy is to restore sustainable economic growth and to preserve and strengthen the free trading system. The world economy is poised for a sustained recovery: inflation rates in most major countries have receded; nominal interest rates have fallen sharply; inventory rundowns are largely complete.

Solid, observable U.S. recovery is one critical ingredient missing for world economic expansion. We believe the U.S. recovery is now getting underway, as evidenced by the recent drop in unemployment and upturns in orders and production in some key industries. Establishing credible growth in other industrial economies is also important and we believe the base for recovery is being laid abroad as well.

However, both we and others must exercise caution at this turning point. Governments must not give in to political pressures to stimulate their economies too quickly through excessive monetary or fiscal expansion. A major shift at this stage could place renewed upward pressure on inflation and interest rates.

In addition, rising protectionist pressures, both in the United States and elsewhere, pose a real threat to global recovery and to the resolution of the debt problem. When one country takes protectionist measures hoping to capture more than its fair share of world trade, other countries will retaliate. The result is that world trade shrinks, and rather than any one country gaining additional jobs, everybody loses. More importantly for current debt problems, we must remember that export expansion by countries facing problems is crucial to their balance of payments adjustment efforts. Protectionism cuts off the major channel of such expansion. That adjustment is essential to restoring problem country debtors to sustainable balance of payments positions and avoiding further liquidity crises -- and as we have seen, it is therefore essential to the economic and financial health of the United States.

The only solution is a stronger effort to resist protectionism. As the world's largest trading nation, the United States carries a major responsibility to lead the world away from a possible trade war. The clearest and strongest signal for other countries would be for the United States to renounce protectionist pressures at home and to preserve its essentially free trade policies. That signal would be followed, and would reinforce, continued U.S. efforts to encourage others to open their markets, and would in turn be reinforced by IMF program requirements for less restrictive trade policies by borrowers.

The Role and Resources of the IMF

I have stressed the role of the International Monetary Fund in dealing with the current financial situation, and now I would like to expand on that point. The IMF is the central official international monetary institution, established to promote a cooperative and stable monetary framework for the world economy. As such, it performs many functions beyond the one we are most concerned with today -- that of providing temporary balance of payments financing in support of adjustment. These include monitoring the appropriateness of its members' foreign exchange arrangements and policies, examining their economic policies, reviewing the adequacy of international liquidity, and providing mechanisms through which its member governments cooperate to improve the functioning of the international monetary system.

In that context, it becomes clearer that IMF financing is provided only as part of its ongoing systemic responsibilities. Its loans to members are made on a temporary basis in order to safeguard the functioning of the world financial system -- in order to provide borrowers with an extra margin of time and money which they can use to bring their external positions back into reasonable balance in an orderly manner, without being forced into abrupt and more restrictive measures to limit imports. The conditionality attached to IMF lending is designed to assure that orderly adjustment takes place -- and that the borrower is restored to a position which will enable it to repay the IMF over the medium term. In addition, a borrower's agreement with the IMF on an economic program is usually viewed by financial market participants as an international "seal of approval" of the borrower's policies, and serves as a catalyst for additional private and official financing.

The money which the IMF has available to meet its members' temporary balance of payments financing needs comes from two sources: quota subscriptions and IMF borrowing from its members. The first source, quotas, represents the Fund's main resource base and presently totals some SDR 61 billion, or about $67 billion at current exchange rates. The IMF periodically reviews the adequacy of quotas in relation to the growth of international transactions, the size of likely payments imbalances and financing needs, and world economic prospects generally.

At the outset of the current quota discussions in 1981, many IMF member countries favored a doubling or tripling of quotas, arguing both that large payments imbalances were likely to continue and that the IMF should play a larger intermediary role in financing them. While agreeing that quotas should be adequate to meet prospective needs for temporary financing, the United States felt that effective stabilization and adjustment measures should lead to a moderation of payments imbalances. We did not support the view that the IMF should become a regular source of financing, a more or less permanent intermediary between borrowers and lenders. Nor did we feel that a massive quota increase would be an efficient way to equip the IMF to deal with sudden and potentially major financing problems that could threaten the stability of the system as a whole, and for which the IMF's resources were inadequate.

Accordingly, the United States proposed a dual approach to strengthening IMF resources:

-- First, a quota increase which, while smaller than many others had wanted, could be expected to position the IMF to meet members' needs for temporary financing in normal circumstances.

-- Second, establishment of a contingency borrowing arrangement that would be available to the IMF on a stand-by basis for use in situations threatening the stability of the system as a whole.

This approach has been adopted by the IMF membership, in agreements reached by the major countries in the Group of Ten in mid-January, and by all members at the IMF's Interim Committee meeting last week.

The agreed increase in IMF quotas is 47 percent, an increase from SDR 61 billion to SDR 90 billion (in current dollar terms, an increase from $67 billion to $99 billion). The proposed increase in the U.S. quota is SDR 5.3 billion ($5.8 billion at current exchange rates) representing 18 percent of the total increase.

The Group of Ten, working with the IMF's Executive Board, has agreed to an expansion of the IMF's General Arrangements to Borrow from the equivalent of about SDR 6.5 billion at present to a new total of SDR 17 billion, and to changes in the GAB to permit its use, under certain circumstances, to finance drawings on the IMF by any member country. Under this agreement, the U.S. commitment to the GAB would rise from $2 billion to SDR 4.25 billion, equivalent to an increase of $2.6 billion at current exchange rates.

We believe this expansion and revision of the GAB offers several important attractions and, as a supplement to the IMF's quotas, greatly strengthens the IMF's role as a backstop to the system:

-- First, since GAB credit lines are primarily with countries that have relatively strong reserve and balance of payments positions, they can be expected to provide more effectively usable resources than a quota increase of comparable size. Consequently, expansion of the GAB is a more effective and efficient means of strengthening the IMF's ability to deal with extraordinary financial difficulties than a comparable increase in quotas.

-- Second, since the GAB will not be drawn upon in normal circumstances, this source of financing will be conserved for emergency situations. By demonstrating that the IMF is positioned to deal with severe systematic threats, an expanded GAB can provide the confidence to private markets that is needed to ensure that capital continues to flow, thus reducing the risk that the problems of one country will affect others.

-- And third, creditors under this arrangement will have to concur in decisions on its activation, ensuring that it will be used only in cases of systemic need and in support of effective adjustment efforts by borrowing countries.

Annex A to my statement contains the texts of the relevant Interim Committee and Group of Ten communiques. These substantive agreements will be codified in formal Governors and Executive Board decisions in the next few weeks. In sum, the proposed increase in U.S. commitments to the IMF totals SDR 7.7 billion -- SDR 5.3 billion for the increase in the U.S. quota and SDR 2.4 billion for the increase in the U.S. commitment under the GAB. At current exchange rates, the dollar equivalents are $8.4 billion in total, $5.8 billion for the quota increase and $2.6 billion for the GAB increase.

We believe these steps to strengthen the IMF, if enacted, will safeguard the IMF's ability to respond effectively to current financial problems. Given the financing needs we foresee, we feel it is important that the increases be implemented by the end of this year. Without such a timely and adequate increase in IMF resources, the ability of the monetary system to weather debt and liquidity problems will be impaired, at substantial direct and indirect cost to the United States.

The IMF is essentially a non-political institution, with membership open to any country judged willing and able to meet the obligations of membership. But this does not mean that U.S. political and security interests are not served by the IMF. On the contrary -- it serves our interests well by containing economic problems which could otherwise spread through the international community; minimizing political instability in countries facing the inevitable social and economic dislocations which accompany adjustment; and supporting open, market-oriented economic systems consistent with Western political values. Judged on this criterion, U.S. appropriations for the IMF can be an excellent investment if they can help to avoid political upheaval in countries of critical interest to the United States.

While this is the first time I have appeared before Congress to support these specific agreements and proposals to increase IMF resources, the general issues and outline are familiar to members of the Committee. Many of you have expressed reservations or questions about this proposal, and I would like to discuss the main concerns now.

Is the IMF "Foreign Aid"?

Many perceive money appropriated for IMF use to be just another form of foreign aid, and question why we should be providing U.S. funds dollars to foreign governments. Let me assure you that the IMF is <u>not</u> a development institution. It does not finance dams, agricultural cooperatives, or infrastructure projects. I have already made the point that the IMF <u>is</u> a <u>monetary</u> institution. Only one of its functions is providing balance of payments financing to its members in order to promote orderly functioning of the monetary system, and only then on a temporary basis, on medium-term maturities, after obtaining agreement to the fulfillment of policy conditions. We have been working very hard with the IMF to ensure that both the effectiveness of IMF policy conditions, and the temporary nature of its financing, are safeguarded. In this way, the Fund's financing facilities will continue to have a revolving nature and to promote adjustment.

IMF conditionality has been controversial over the years, with strong opinions on both sides. Some observers have worried that conditionality is so weak and ineffective that conditional lending is virtually a giveaway. Others believe that conditionality is too tight -- that it imposes unnecessary hardship on borrowers, and stifles economic growth and development.

Such generalizations reflect a misunderstanding of IMF conditionality. When providing temporary resources to a country faced with external financing problems, the IMF seeks to assure itself that the country is pursuing policies that will enable it to live within its means -- that is, within its ability to obtain foreign financial resources. It is this that determines the degree of adjustment that is necessary. It is often the case that appropriate economic policies will strengthen a country's borrowing capacity, and result in both higher import growth and higher export growth. In this connection, I would cite the example of Mexico as an immediate case in point.

Mexico is our third largest trading partner, after Canada and Japan. And, as recently as 1981, it was a partner with whom we had an export boom and a substantial trade surplus, exporting goods to meet the demands of its rapidly growing population and developing economy. This situation changed dramatically in 1982, as Mexico began experiencing severe debt and liquidity problems. By late 1982, Mexico no longer had access to financing sufficient to maintain either its imports or its domestic economic activity. As a result, U.S. exports to Mexico dropped by a staggering 60 percent between the fourth quarter of 1981 and the fourth quarter of 1982. Were our exports to Mexico to stay at their depressed end-1982 levels, this would represent a $10 billion drop in exports

exports to our third largest market in the world. Because the financing crunch got worse as the year wore on, totals for the full year 1982 don't tell the story quite so dramatically -- but even they are bad enough. Our $4 billion trade surplus with Mexico in 1981 was transformed into a trade deficit of nearly $4 billion in 1982, due mainly to an annual-average drop in U.S. exports of one-third. (Chart I.) This $8 billion deterioration was our worst swing in trade performance with any country in the world, and it was due almost entirely to the financing problem.

We believe that now this situation will start to turn around, and we can begin to resume more normal exports to Mexico. If this happens, it will be due in large part to the fact that, late in December, an IMF program for Mexico went into effect; and that program is providing the basis not only for IMF financing, but for other official financing and for a resumption of commercial bank lending as well. Mexico must make difficult policy adjustments if it is to restore creditworthiness. The Mexican authorities realize this and are embarked on a courageous program. But the existence of IMF financing and the other financing associated with it will permit Mexico to resume something more like a normal level of economic activity and imports while the adjustment takes place in an orderly manner. Without the IMF program, all we could look forward to would be ever-deepening depression in Mexico and still further declines in our exports to that country.

There is another aspect of the distinction between IMF financing and foreign aid which we should be very clear on, since it goes to the heart of U.S. relations with the Fund. All IMF members provide financing to the IMF under their quota subscriptions, and all -- industrial and developing alike -- have the right to draw on the IMF. Quota subscriptions form a kind of revolving fund, to which all members contribute and from which all are potential borrowers.

As an illustration, in practice our quota subscription has been drawn upon many times -- and repaid -- over the years for lending to other IMF members. We in turn have drawn on the IMF on 24 occasions -- most recently in November 1978 -- and our total cumulative drawings, amounting to the equivalent of $6.5 billion, are the second largest of any member (the United Kingdom has been the largest user of IMF funds). (U.S. drawings on the IMF are described at Annex B.)

<u>Why Spend Money on the IMF?</u>

Another major concern with the proposals to increase IMF resources is that, in this period of budgetary stringency, many believe we would be better advised to spend the money at home. There is also some feeling that if we were to get the U.S. economy moving forward again, the international financial problem would take care of itself. I think I've already been through part of the response to these concerns when I described the large and growing impact which foreign trade now has on American growth and employment. We will do what is necessary domestically to strengthen our economy. But we will leave a major threat to domestic recovery unaddressed if we do not act to resolve the international financial situation. The direct impact alone of international developments on our economy is so large that, were the international situation not to improve, there would at a minimum be a tremendous drag on our economic recovery.

It is true that an improving U.S. economy is going to help other nations, both through our lower interest rates and through an expanding U.S. market for their exports -- providing of course that we don't cut them off from that market. But they also have an immediate, short-run financing crunch to get through, and if we don't handle that right there are substantial downside risks for the United States.

This might also be the right context in which to discuss how U.S. participation in the increase in IMF resources would affect the Federal budget and the Treasury's borrowing requirements. Under budget and accounting procedures adopted in connection with the last IMF quota increase, in consultation with the Congress, both the increase in the U.S. quota and the increase in the U.S. commitment under the GAB will require authorization and appropriation by the Congress. Because the United States receives a liquid, interest-earning reserve claim on the IMF in connection with our actual transfers of cash to the IMF, such transfers do not result in net budget outlays or an increase in the Federal budget deficit.

Actual cash transactions with the IMF, under our quota subscription or U.S. credit lines, do affect Treasury borrowing requirements. The amount in any year depends on a variety of factors, including the rate of use of IMF resources; the degree to which the dollar is used in IMF drawings and repayments to the IMF; and whether the United States itself draws on the IMF. An analysis appended to this statement at Annex C presents data on the impact of U.S. transactions between 1970 and 1982 on Treasury borrowing requirements. Although there have been both increases and decreases in Treasury borrowing requirements from year to year, on average there have been increases amounting to $454 million annually over the entire 13 year period, for a cumulative total of over $6 billion. The rate has picked up in the last two years of heavy IMF activity, as would be expected; but the total is still relatively small -- the $454 million annual impact is only a small part of the $54 billion annual average Federal borrowing requirement over the same period, and the $6 billion cumulative impact compares with an outstanding Federal debt of $1.2 trillion at the end of 1982. These figures also serve to demonstrate the revolving nature of the IMF.

<u>Is the IMF a Bank "Bail-Out"?</u>

I also know there is a widespread concern that an increase in IMF resources will amount to a bank bail-out at the expense of the American taxpayer. Many would contend that the whole debt and liquidity problem is the fault of the banks -- that they've dug themselves and the rest of us into this hole though greed and incompetence, and now we intend to have the IMF take the consequences off their hands. This line of argument is dangerously misleading, and I would like to set the record straight.

First, the steps that are being taken to deal with the financial problem, including the increase in IMF resources, require continued involvement by the banks. Far from allowing them to cut and run, orderly adjustment requires <u>increased</u> bank lending to troubled LDCs that are prepared to adopt serious economic programs. That is exactly what is happening.

And it is not a departure from past experience. I have had Treasury staff review IMF program experience in the 20 countries which received the largest net IMF disbursements in the last few years, to see whether banks had been "bailed out" in the past. Looking at the period from 1977 to mid-1982, they found that for the countries which rely most heavily on private bank financing, IMF programs have been followed up by new bank lending much greater than the amount disbursed by the Fund itself. This also holds true for the 20 countries as a group: net IMF disbursements to this group during the period were $11.5 billion, while net bank lending totalled $49.7 billion, resulting in a ratio of 4.3 to 1 during this period.

The second point I would like to stress here is the notion that the increase in IMF resources is coming mainly from the United States. The U.S. share in the increase in IMF resources is 18 percent -- which obviously means other countries are putting up the remaining 82 percent, the great bulk of the increase. By putting up 18 percent of the increase, we will maintain our voting share at just over 19 percent. The principle of weighted voting on which the IMF operates has been key to its effectiveness over the years and to ensuring that we have a voice and vote comparable to the share of resources we provide. Major policy decisions -- such as those just taken on the quota increase -- require an 85 percent majority vote, which means that we have a veto over all such decisions. Some of our allies would claim that we aren't pulling our own weight -- that our stake in world trade and finance is bigger than the share of resources we are proposing to put into the IMF would indicate.

The third point I would like to make is that the whole debt and liquidity problem cannot fairly be said to be the fault of the commercial banks. In fact, the banking system as a whole performed admirably over the last decade, in a period when there were widespread fears that the international monetary system wou fall apart for lack of financing in the aftermath of the oil shocks. The banks managed almost the entire job of "recycling" the OPEC surplus and getting oil importers through that difficul period. Some of the innovations and decisions that banks made in the process, which seemed rational and necessary at the time to them and to others, may seem doubtful in retrospect, given the way the world economic environment changed. But I think we can agree that governments have had a great deal to do with shaping that environment.

All of this is not to say that there aren't lessons to be learned in the banking area -- there clearly has been an element of lack of prudence in lending decisions, and of overlending. S we should be asking ourselves: What is there that banks could b doing to improve their screening of foreign loans? What is ther that bank regulators could do to improve on their analysis of country risk, examination of bank exposure, and consultations with senior management?

Our basic starting point in addressing these questions is a belief that the U.S. government should not get into the business of dictating the lending practices of private banks. Doing so would inject a political element into what should be business decisions, and would potentially expose the government to liabil for covering loans that were not repaid on time. Moreover, in general it is bank managements, which have direct experience and a responsibility to their shareholders and depositors to motivat them, that are in the best position to make lending decisions.

In 1979, the bank regulatory agencies (the Federal Reserve, Comptroller of the Currency and the FDIC) instituted a new system for evaluating country risk, which has four elements. The first is a statistical reporting system designed to identify country exposures at each bank, and to enable regulators to monitor those exposures. Second is an evaluation of each bank's internal system for managing country risk, aimed at encouraging more systematic review of prospective loans. Third, where there is a judgment by regulators that a country has interrupted its debt service payments, or is about to do so, all loans to that country may be "classified" as substandard, doubtful, or a total loss, and such "classification" may trigger an obligation by the bank to set aside precautionary loan loss reserves. Fourth, bank examiners review and comment upon each bank's large foreign lending exposures, drawing upon the findings of an interagency committee of country analysts.

There are several possible changes that could be made in the regulatory environment. One would be to set up formal limits on each bank's exposure in different countries by law or regulation, in effect setting up "single country" limits analogous to the "single borrower" limits which are already used. Such limits on country exposure would necessarily be highly arbitrary and unable to distinguish among the capabilities of different banks or among the size and financial health of different countries, especially if applied by law. If applied judgmentally, on the other hand, such "single country" limits would require that the U.S. government make controversial economic and political judgments about other countries. The present system, which uses various ratios of exposure as a percentage of capital as a threshhold point for commenting upon loans to certain countries, is more flexible and should be a useful basis for our future procedures. More intensive discussion with senior bank management during the examination process would probably be desirable.

Another possibility, which has been discussed with banks here and abroad, would be to require banks to meet specific criteria in establishing precautionary loan loss reserves agains troubled loans, or even just against particularly large ones. Current procedures are not uniform across banks, and since setti aside such reserves reduces current earnings, there is some reluctance to do so unless absolutely required. Also, in the case of "sovereign loans" to public-sector borrowers, the argume is often made that the borrower cannot simply "disappear" or go bankrupt in the sense that a private borrower could, so that interest and principal arrears are certain to be recovered. However, the current situation shows that sovereign borrowers, too, can have protracted difficulties, and that their difficulti can have a more abrupt impact than would be the case if provisio against possible loan loss had been made more routinely over tim

Additionally, there is the question of whether banks' curre disclosure of the size, distribution, terms, and status of their foreign loans is sufficient. Depositors have a legitimate inter in knowing what banks are doing with the money entrusted to them Regulatory agencies have been considering this issue, and there has been some movement toward greater disclosure. Here again, there is reason to proceed with caution. When foreign lending is in vogue, the disclosure that competiting banks are expanding their foreign loans might generate pressure for other banks to d the same, even where it is against their best judgment. When attitudes move the other way, markets may overreact on the basis of hasty or naive readings of the data. The desire of borrowers for confidentiality and other competitive considerations may also limit the degree of disclosure.

Both in the banking regulatory agencies, and at the Treasury, we will be reviewing these and other issues to see what changes might be desirable. We need to be careful in determining how to deal with such a sensitive and central part of our economy. Any decisions in this area will have important implications both for resolving the present situation, and for the evolution of the banking system in the future. Chairman Volcker, Comptroller Conover, and FDIC President Isaac are scheduled to appear before a Subcommittee of the Banking Committee on Thursday to discuss these matters in more detail.

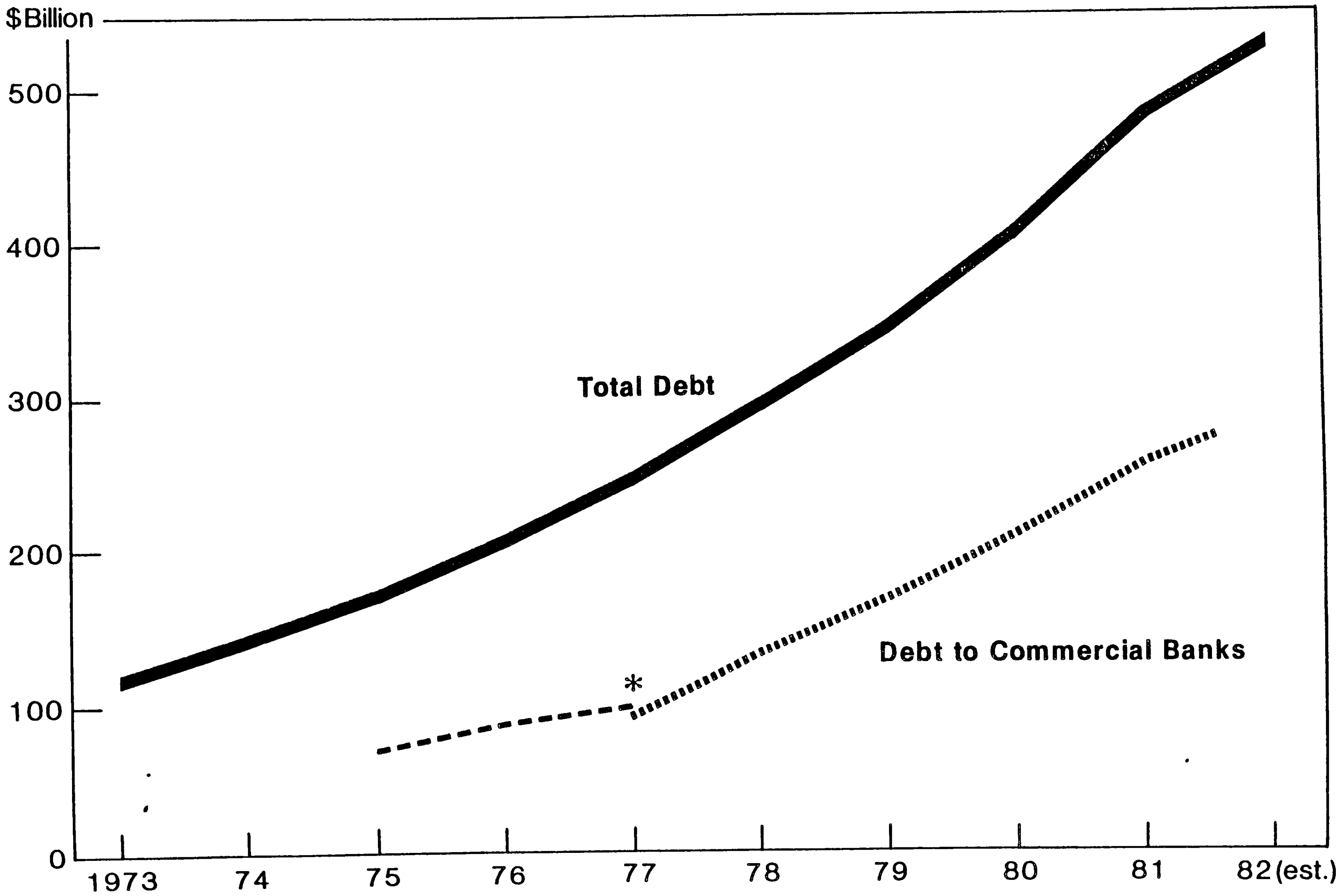
Conclusion

The IMF plays a crucial role in the solution to current debt and liquidity problems, and in providing the environment for world recovery. It is absolutely essential that the proposed increase in IMF resources become effective by the end of this year, to enable the IMF to meet these responsibilities. Prompt U.S. approval is important not only because the financing is needed, but also because it would be a sign of confidence to other governments and to the public, and would help lay to rest concerns about the risks to global recovery.

But most importantly, timely approval of these proposals is essential to our own economic interests -- to the prospects for American businesses and American jobs. The legislation will be submitted to you in a very few days. I urge that you give it prompt and favorable consideration.

CHART A

OUTSTANDING FOREIGN DEBT OF OIL-IMPORTING LDCs



* Series break.

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CHART B

NET NEW LENDING BY COMMERCIAL BANKS TO OIL-IMPORTING LDCs

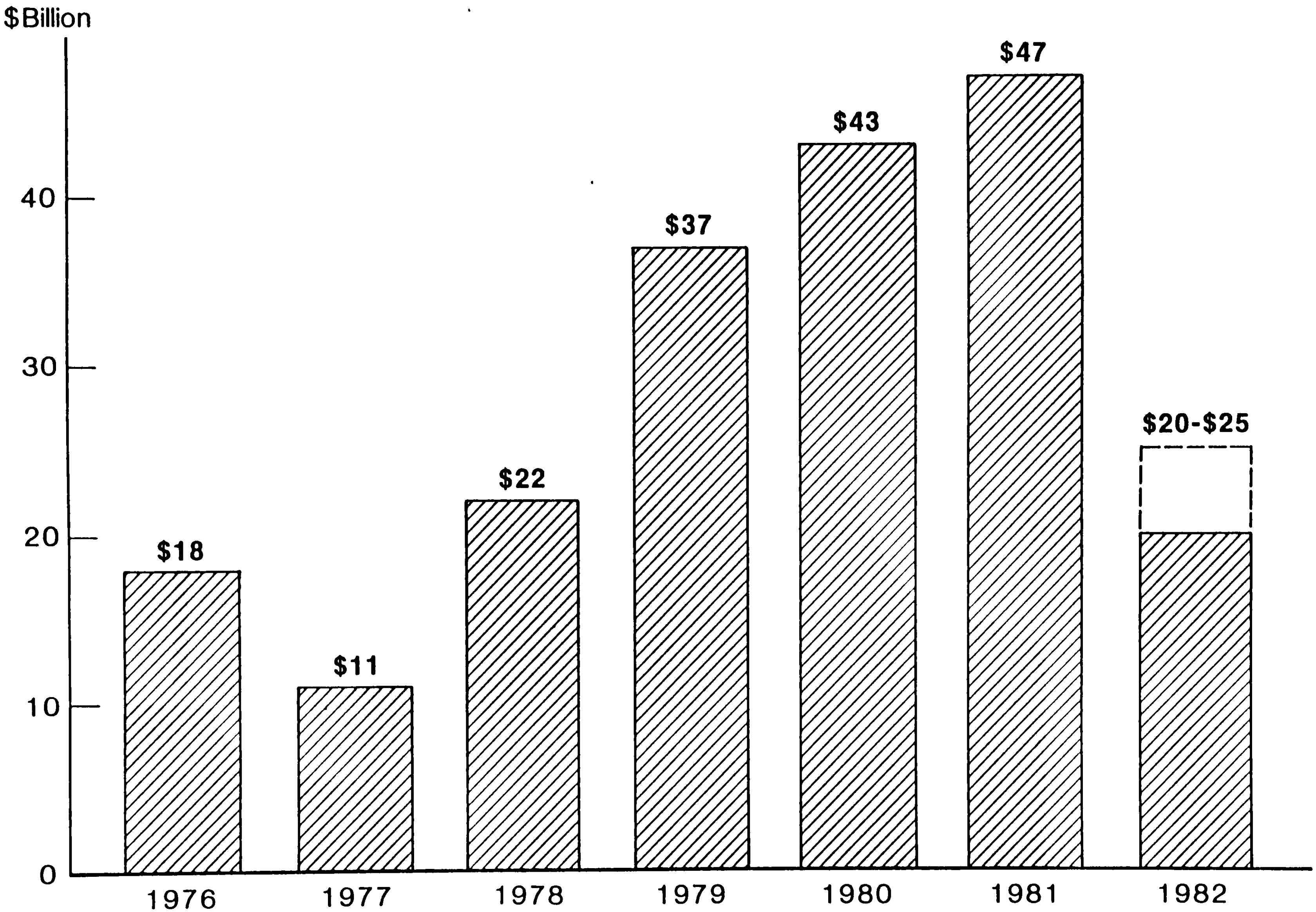

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CHART C

GROWTH OF U.S. AND WORLD EXPORT VOLUME

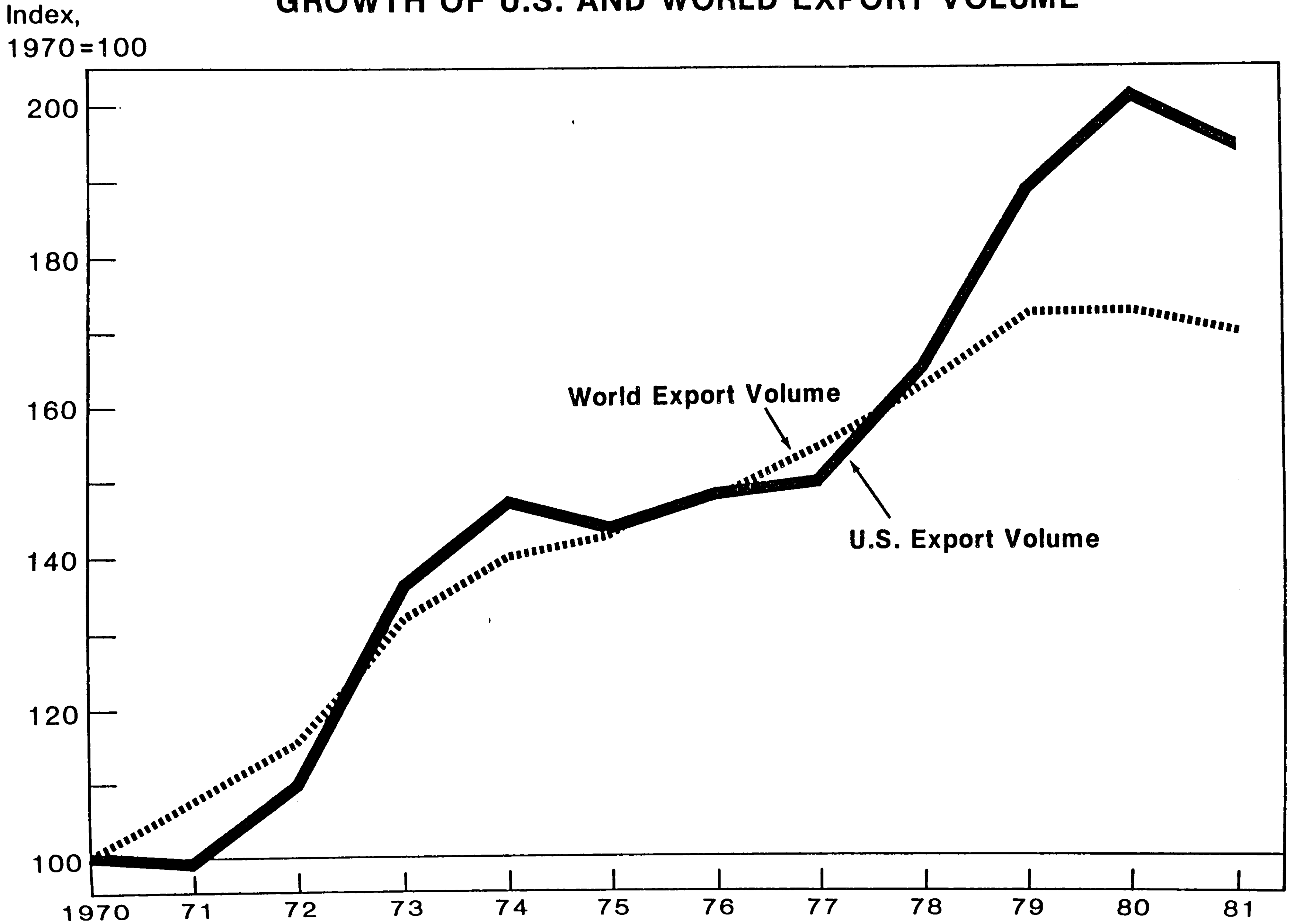

CHART D

SHARE OF U.S. EXPORTS IN TOTAL U.S. GOODS OUTPUT

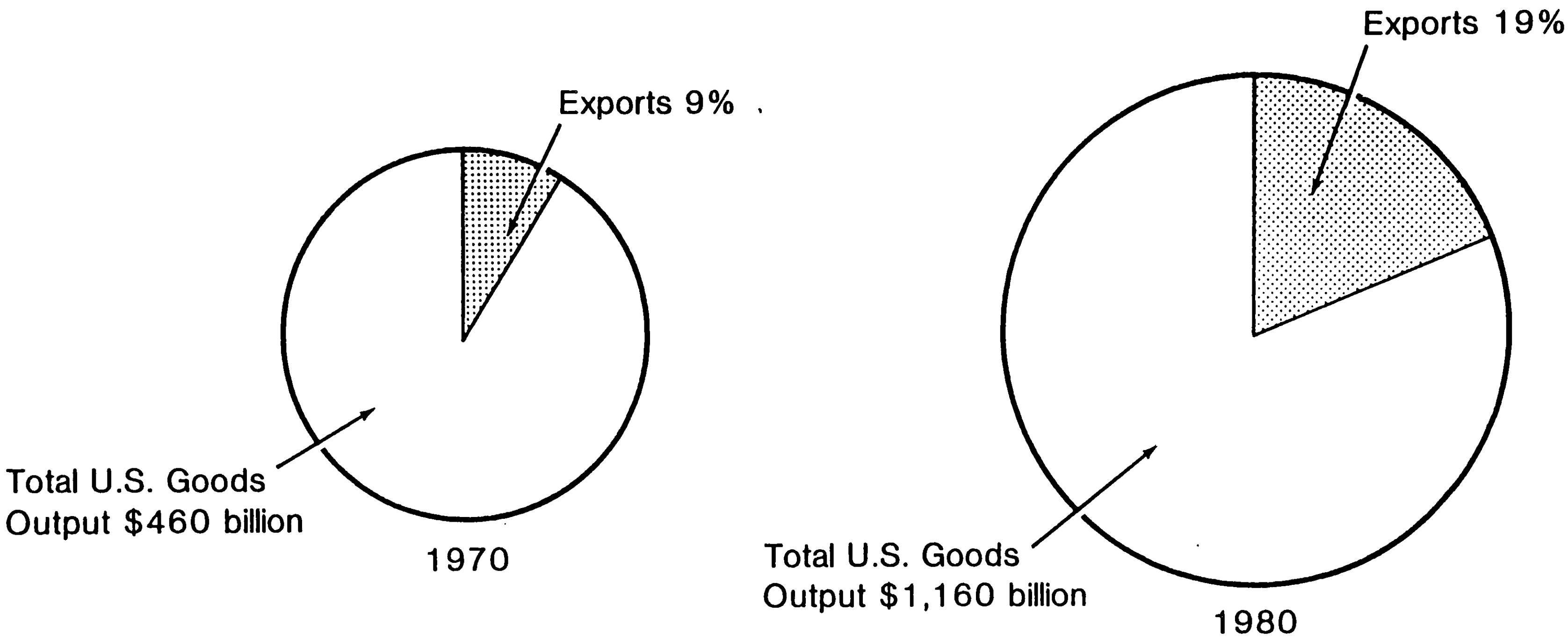

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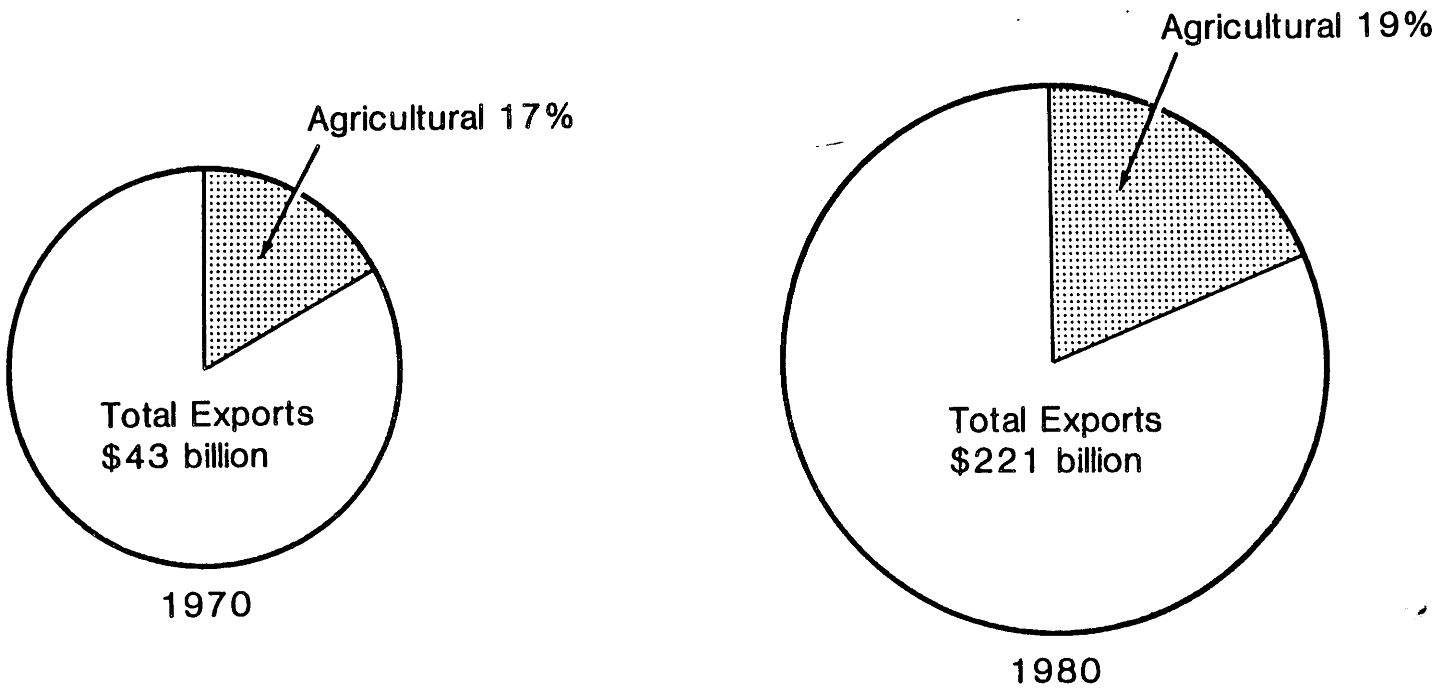
CHART E

U.S. AGRICULTURAL EXPORTS

Share in Total U.S. Exports:



	1970	1980
Net U.S. Agricultural Trade Balance:	Surplus of $1.6 billion	Surplus of $24.3 billion

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2-11-83

CHART F

U.S. TRADE BALANCE IN SERVICES

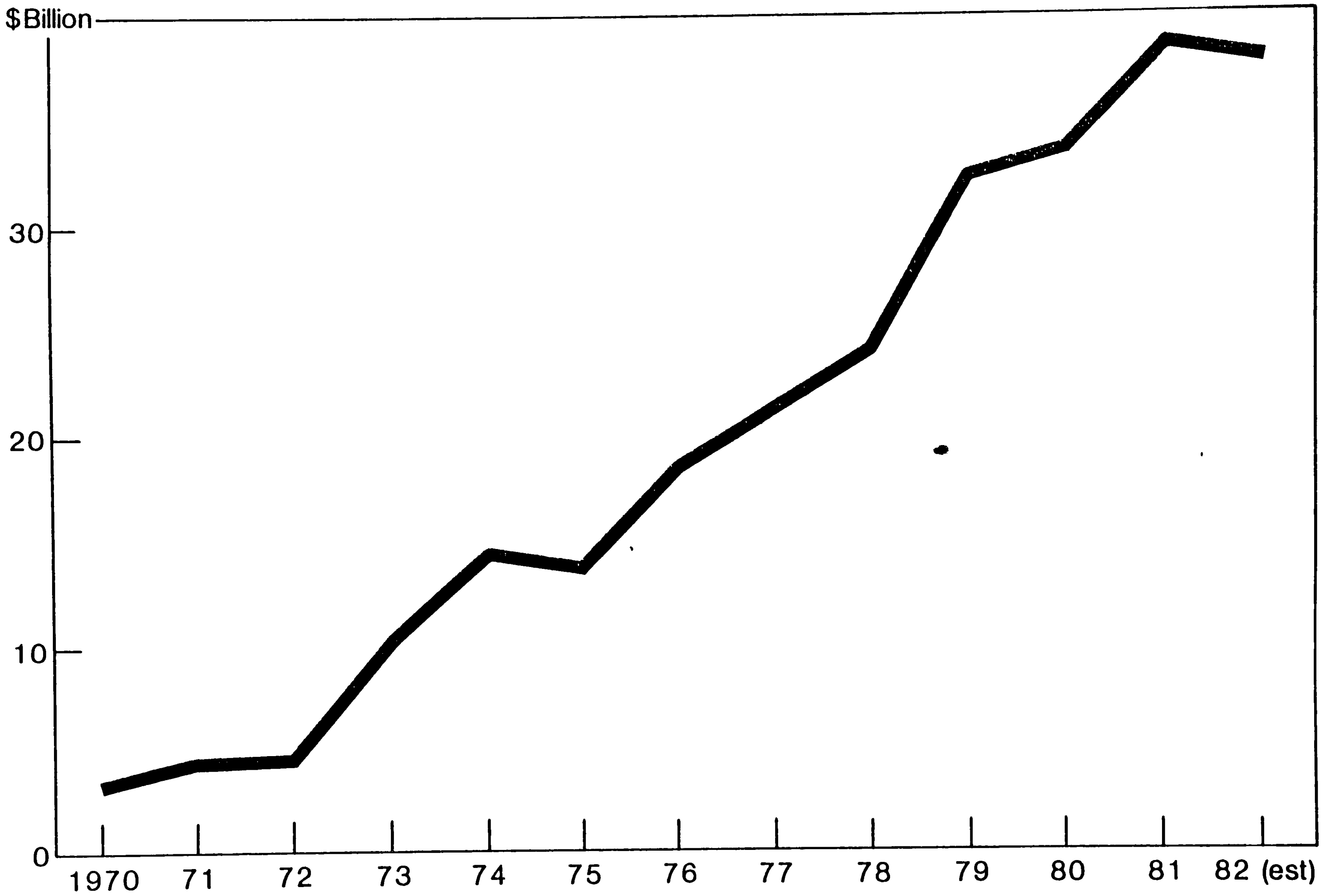

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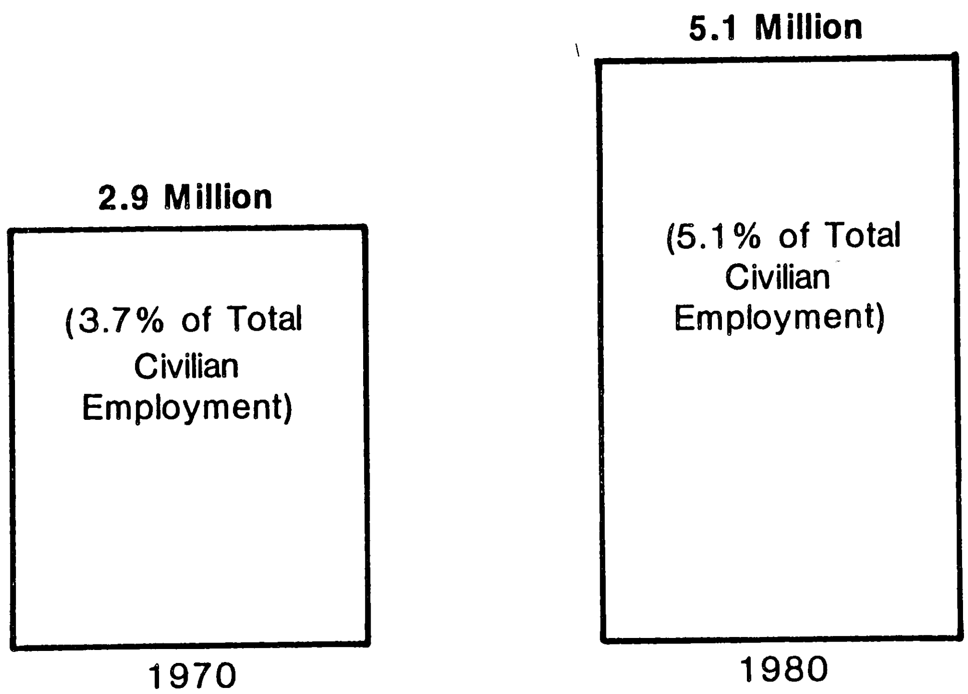
CHART G

U.S. EXPORT-RELATED JOBS



As of 1980, each $1 billion of U.S. exports was estimated to result in 24,000 jobs.

Source: Commerce Department (ITA) estimates.

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2-11-83

CHART H

U.S. EXPORTS TO OIL-IMPORTING LESS DEVELOPED COUNTRIES

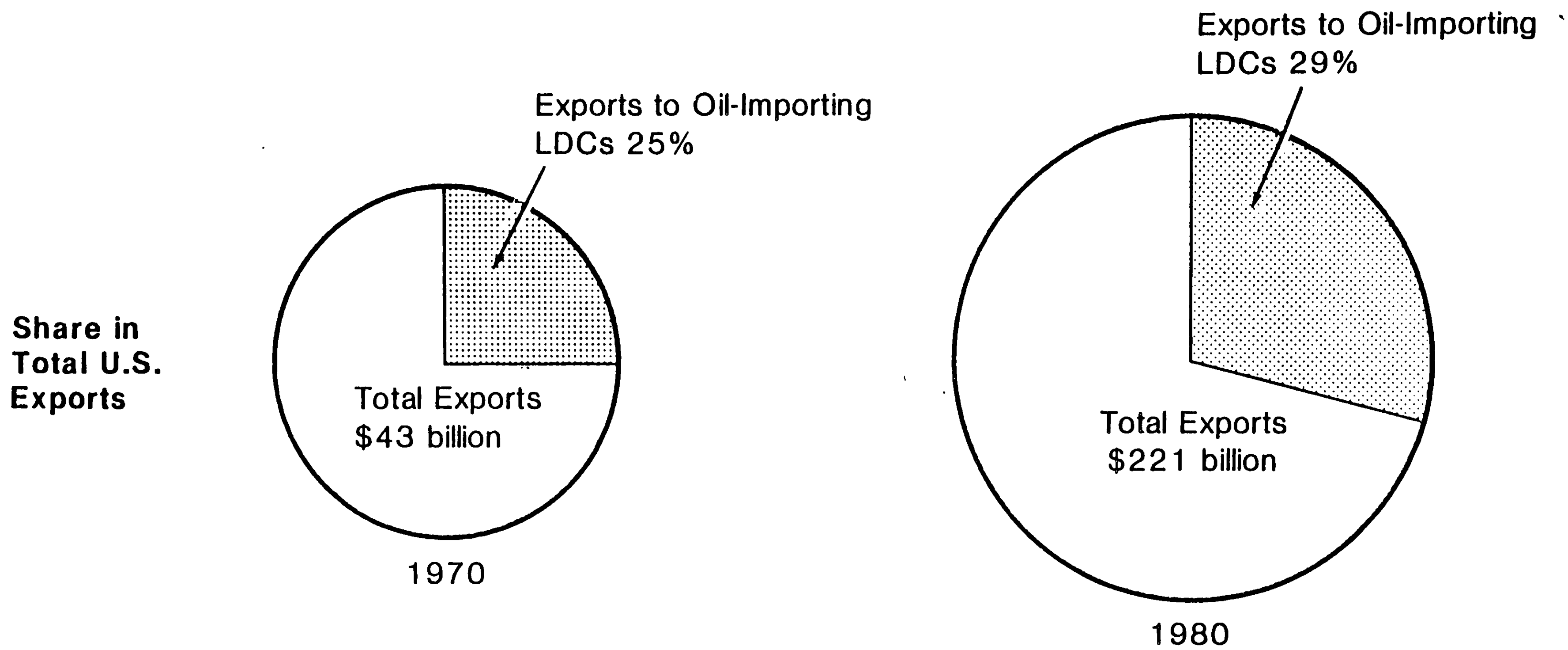

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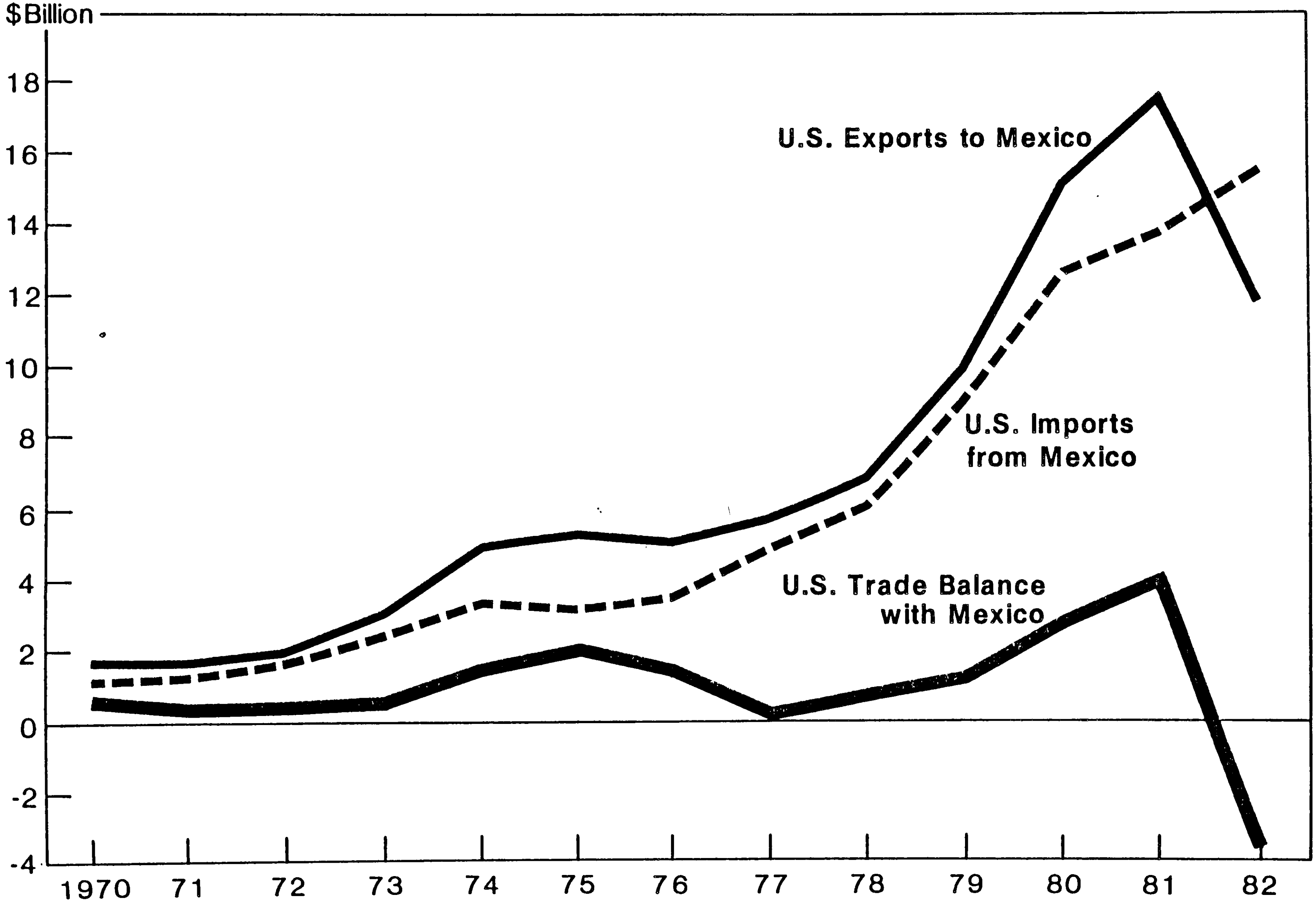
CHART I

U.S. TRADE WITH MEXICO



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INTERNATIONAL MONETARY FUND

Press Release NO. 83/11

FOR IMMEDIATE RELEASE
February 11, 1983

Press Communiqué of the Interim Committee of the Board of Governors of the International Monetary Fund

1. The Interim Committee of the Board of Governors of the International Monetary Fund held its twentieth meeting in Washington, D.C., on February 10 and 11, 1983, under the chairmanship of Sir Geoffrey Howe, Chancellor of the Exchequer of the United Kingdom. Mr. Jacques de Larosière, Managing Director of the International Monetary Fund, participated in the meeting. The meeting was also attended by observers from a number of international and regional organizations and from Switzerland.

2. The Committee discussed the World Economic Outlook and the policies needed to cope with the difficult problems faced by most members of the Fund.

The Committee noted that estimated rates of both growth of output and inflation had been revised downward since its previous meeting in September 1982. Anxiety was expressed at the high level of unemployment and the weakness of investment and world trade, against the background of only limited indications of economic recovery. At the same time, the Committee welcomed the further progress made by some of the larger industrial countries in their fight against inflation, as well as the reduction in interest rates that had been facilitated by this progress--developments that were providing the basis for a sustainable recovery in economic activity.

Believing that successful handling of the inflation problem is a necessary--albeit not sufficient--condition for sustained growth over the medium term, the Committee urged national authorities, in their efforts to promote sustained recovery, to avoid measures that might generate harmful expectations with regard to inflation. The importance of reducing fiscal deficits in a number of countries was also emphasized. Otherwise, the Committee noted, high real interest rates detrimental to the process of recovery could be generated by market expectations regarding government borrowing requirements.

It was the Committee's view that, in several major industrial countries where inflation remained relatively high, present circumstances called for continued restraint in monetary and fiscal policies, along with effective implementation of the incomes policies now in place. It was felt, however, that conditions for economic recovery had improved in those large industrial countries that have been able to achieve the greatest measure of success in reducing and controlling inflation. This success--and the reduction in interest rates that it has permitted--provided the basis, within the pursuit of counter-inflationary monetary and fiscal policies, for greater real growth of activity. The transition to a more stable path of real growth would be further facilitated by determined efforts to reduce market rigidities and structural imbalances.

The Committee deplored the upsurge of protectionist pressures in the past year or two. It stressed the paramount importance of resisting these pressures and, indeed, rolling them back.

The unsatisfactory situation facing non-oil developing countries was a source of particular concern to the Committee, which noted that growth rates in these countries, after averaging about 6 per cent in the 1960s and early 1970s, had averaged only 2 1/2 per cent during the past two years and were not expected to show much improvement in 1983. The Committee also observed that the modest recent increases in output, which were barely sufficient to keep pace with rapid population growth, had been achieved against a background of deteriorating terms of trade, sluggish markets for exports, high interest rates in international financial markets, and strains in the financing of current account deficits. These conditions had necessitated a sharp compression of imports by the non-oil developing countries--which, in turn, had been achieved at the cost of lower investment and growth.

Noting the extent of the external adjustment already achieved by many non-oil developing countries and the uncertainties that most such countries face in financing their current account deficits, the Committee attached great importance to the continuing provision of both official development assistance and private banking flows on an adequate scale, and it welcomed the special role recently played by the Fund in this connection.

More generally, the Committee stressed the enhanced importance, in current circumstances, of the Fund's role in providing its balance of payments assistance to member countries that engage in adjustment programs and in exercising firm surveillance over policies, and also the need to equip the Fund with adequate resources to perform this role.

3. The Committee, noting the progress made by the Executive Board on the various issues of the Eighth General Review of Quotas, focused its attention on the remaining issues, and took satisfaction in being able to reach the following agreement on the subject of quotas:

(a) The total of Fund quotas should be increased under the Eighth General Review from approximately SDR 61.03 billion to SDR 90 billion (equivalent to about US$ 98.5 billion).

(b) Forty per cent of the overall increase should be distributed to all members in proportion to their present individual quotas, and the balance of sixty per cent should be distributed in the form of selective adjustments in proportion to each member's share in the total of the calculated quotas, i.e., the quotas that broadly reflect members' relative positions in the world economy.

(c) Twenty-five per cent of the increase in each member's quota should be paid in SDRs or in usable currencies of other members.

The Committee considered the possibility of a special adjustment of very small quotas, i.e., those quotas that are currently less than SDR 10 million. It was agreed to refer this matter to the Executive Board for urgent consideration in connection with the implementation of the main decision.

4. The question of the limits on access to the Fund's resources was raised in the Committee. It was noted that the Executive Board will review this matter before June 30, 1983. The Committee invited the Executive Board to take note of the views expressed in the Committee by those favoring maintenance of the present enlarged limits in terms of multiples of quotas and also by those stressing the need to have regard to developments in the Fund's liquidity. It also invited the Managing Director to report on this matter at the next meeting of the Committee.

5. The Committee noted the recent decision of the Finance Ministers and Central Bank Governors of the participants in the General Arrangements to Borrow (GAB) to support an increase in the total amount of the commitments under these Arrangements to SDR 17 billion (equivalent to about US$19 billion) and to make the resources of these Arrangements available to the Fund to finance also purchases by nonparticipants when the Fund faces an inadequacy of resources arising from an exceptional situation involving a threat to the stability of the international monetary system. In this connection, the Committee welcomed the intention of Switzerland to become a full participant in the Arrangements, through the Swiss National Bank, with a credit commitment of SDR 1,020 million.

The Committee also welcomed the willingness of Saudi Arabia to provide resources to the Fund, in association with the GAB, and for the same purposes as those of the GAB. They noted with satisfaction the progress that is being made in setting out the detailed features of this association.

6. The members of the Committee requested the Executive Board to adopt, before the end of February 1983, the necessary decisions and other actions to implement the consensus reached in the Committee. They also agreed to urge the governments of their constituencies to act promptly so that the proposals for the increase in the Fund's resources could be made effective by the end of 1983.

7. The Committee considered again the question of allocations of SDRs in the current, i.e., the fourth, basic period which began on January 1, 1982. Noting the developments since its Toronto meeting, the Committee agreed that the matter should be reexamined as soon as possible. It, therefore, requested the Executive Board to review the latest trends in growth, inflation and international liquidity, with a view to enabling the Managing Director to determine, not later than the next meeting of the Interim Committee, whether a proposal for a new SDR allocation could be made that would command broad support among members of the Fund.

8. The Committee agreed to hold its next meeting in Washington, D.C., on September 25, 1983.

January 18, 1983

Group of Ten - Press Communiqué of the Ministers and Governors

1. The Ministers and central bank Governors of the ten countries participating in the General Arrangements to Borrow (GAB) met in Paris on January 18, 1983 under the chairmanship of Mr. Jacques Delors, Minister of Economy and Finance of France. The Managing Director of the International Monetary Fund (IMF), Mr. Jacques de Larosière, took part in the meeting, which was also attended by Mr. F. Leutwiler, President of the Swiss National Bank, Mr. E. Van Lennep, Secretary-General of the Organisation for Economic Cooperation and Development (OECD), Mr. A. Lamfalussy, Assistant General Manager of the Bank for International Settlements, and Mr. F.-X. Ortoli, Vice-President of the Commission of the European Communities.

2. The Ministers and Governors heard a report by the Chairman of their Deputies, Mr. Lamberto Dini, on issues relating to the revision and expansion of the GAB and the Eighth General Review of Quotas of the IMF. They also heard a report by the Chairman of the Working Party No. 3 of the Economic Policy Committee of the OECD, Mr. Christopher Mcmahon, on the world economic outlook.

3. In addressing the world economic situation, the Ministers and Governors welcomed recent successes in the fight against inflation and prospects for further progress. They looked toward sound monetary and fiscal policies and appropriate moderation in the growth in incomes to encourage lower interest rates, expanding trade, higher employment, and durable economic growth. These desirable developments must not be thwarted by trade restrictions or by disruption of the international financial system. At the same time, it was recognized that soundly based growth would itself help ease current tensions. To these ends, the Ministers and Governors affirmed their support for a reinforced cooperation among industrialized countries on economic, financial, and trade policies.

They considered that a sustainable improvement in activity in the industrial countries in 1983 can make an important contribution to a lasting solution of the indebtedness problem of many developing countries and to limiting the unemployment problem in all countries. Therefore, they noted with satisfaction that the competent international organizations will examine whether further steps can be taken to ensure renewed and sustained growth, and will report to the next ministerial councils, notably in the OECD and IMF framework.

4. Against this background, the Ministers and Governors discussed the international financial situation. They noted that, while strains remained in the system and the foreign debt problems of a number of countries were still a cause for real concern, governments and monetary authorities had been cooperating actively and effectively with international monetary institutions and commercial banks to reinforce the stability of the system. In order to ensure the continuing ability of the financial system to cope with existing strains and to facilitate the adjustment process, they strongly supported a substantial increase of resources available to the International Monetary Fund.

5. In light of the foregoing, the Ministers and Governors have decided, subject to the necessary legislative approval, that their aggregate credit commitments under the GAB should be promptly increased--from SDR 6.4 billion to SDR 17 billion (equivalent to an increase from $7.1 billion to about $19 billion). They welcomed the intention of Switzerland to become a full-scale participant in the GAB and decided that necessary adjustments in the arrangements should be made so as to permit the participation of Switzerland at an early date. They also decided an adjustment of the participants' shares in the arrangements so as to reflect better their size and role in the international economy and their ability to provide financial resources. A list of the new credit commitments that have been agreed is attached. They further agreed that in the future the GAB would be available not only for drawings by participants but also for purchases from the Fund for conditional financing for all its members, including members that are not GAB participants, when the Fund was faced with an inadequacy of resources arising from an exceptional situation associated with requests from countries with balance of payments problems of a character or of aggregate size that could pose a threat to the stability of the international monetary system.

6. The Ministers and Governors also looked to the conclusion of arrangements with other countries that might be willing and able to provide substantial resources to the Fund for the same purposes and on terms not unlike those agreed under the GAB. In this regard, the Ministers and Governors welcomed the recent contacts that the Chairman of the Group of Ten, and the

Chairman of the Interim Committee and the Managing Director of the Fund, have had with the authorities of Saudi Arabia. They asked the Chairman of the G-10 Deputies, in collaboration with the Managing Director of the IMF, to resume such contacts as soon as possible.

7. The Ministers and Governors discussed the issues related to the Eighth General Review of Quotas. They agreed that a substantial overall increase was called for. They also recognized the need for a meaningful adjustment of quota shares in the Fund to bring these more in line with the relative position of member countries in the world economy.

8. The Ministers and Governors noted that substantial progress had been made on the Quota Review issues, and were of the view that the conditions were now present for reaching conclusions at the forthcoming meeting of the Interim Committee on February 10-11, 1983. They emphasized the desirability of having new quotas in effect by the end of 1983.

9. The Ministers and Governors expressed their gratitude to the French authorities for their cordial hospitality and for the excellent meeting arrangements.

Attachment

ATTACHMENT

GAB Credit Commitments for G-10 Countries and Switzerland

	In millions of SDRs	Shares in per cent
United States	4,250.0	25.00
Germany	2,380.0	14.00
Japan	2,125.0	12.50
France	1,700.0	10.00
United Kingdom	1,700.0	10.00
Italy	1,105.0	6.50
Canada	892.5	5.25
Netherlands	850.0	5.00
Belgium	595.0	3.50
Sweden	382.5	2.25
Switzerland	1,020.0	6.00
Total	17,000.0	100.00

IMF Drawings by the United States

The United States has drawn on the International Monetary Fund (IMF) on twenty-four occasions over the past 19 years for a total of about SDR 5.8 billion (equivalent to about $6.5 billion at the exchange rates prevailing at the time of each drawing), the second largest amount of cumulative drawings of any IMF member. None of these drawings were subject to IMF policy conditionality, as they involved drawings on the U.S. reserve position in the IMF. Drawings on the reserve position are available automatically upon representation of balance of payments need; do not bear interest and are not subject to repurchase obligations; and do not involve policy conditionality.

The U.S. drawings were for the following purposes: during the 1960's and early 1970's they were designed to limit foreign purchases of U.S. gold reserves; subsequently, they were designed to provide the United States with foreign currencies for the purpose of exchange market operations. These purposes are explained below. A table listing all U.S. drawings is attached.

Drawings During the 1960's and Early 1970's

Under the international monetary arrangements in operation following World War II, each member of the IMF was required to establish and maintain a "par value" for its currency in terms of gold. The United States undertook to fulfill its par value obligations by standing ready to convert dollars held by foreign monetary authorities into gold at the official price of $35 per ounce -- i.e., the par value of the dollar. Other countries met their par value obligations by maintaining exchange rates for their currencies -- directly or indirectly -- in terms of the dollar within narrow margins. In this manner, a structure of currency exchange rates linked to gold was established and maintained.

During the 1950's and 1960's, large payments imbalances, substantial losses of U.S. gold and foreign accumulations of dollar holdings, representing further potential strains on U.S. gold, put increasing strain on this system. Beginning in the early 1960's the United States, in cooperation with foreign monetary authorities, initiated a variety of measures designed to limit pressures on U.S. gold holdings. U.S. drawings on the IMF were an integral part of this program.

In general, IMF drawings provided the United States with foreign currencies that could be used to purchase dollars from foreign monetary authorities and thus reduce demands for conversion of official dollar holdings to gold. The foreign currencies obtained from the IMF were used most often in the following types of transactions:

-- to facilitate repayment of IMF drawings by other countries without necessitating use of U.S. gold;

-- repayment of U.S. short-term currency swaps with foreign central banks; and

-- direct purchases by the United States of foreign official dollar holdings that would otherwise be used to purchase U.S. gold.

Drawings Since the Early 1970's

With the end of the par value/gold convertibility arrangements in the early 1970's, the basic purpose of U.S. drawings from the IMF was to finance U.S. intervention in the exchange markets in support of the dollar. During the 1970's, the U.S. intervened directly in the foreign exchange market, buying and selling foreign currencies for dollars, in order to deal with exchange market pressures on the dollar. The foreign currencies obtained from U.S. drawings in the IMF provided an important source of funds for such intervention. In November 1978, a U.S. drawing of $3 billion of German marks and Japanese yen was a component of a major program of U.S. and foreign intervention in the exchange market to support the dollar.

1/6/82

IMF Drawings by the United States
(SDR Millions)

Date		Amount	Date		Amount
1964:	Feb	125	1968:	March	200
	June	125		Total	200
	Sept	150			
	Dec	125	1970:	May	150
	Total	525		Total	150
1965	March	75	1971:	Jan	250
	July	300		June	250
	Sept	60		Aug	862
	Total	435		Total	1,362
1966	Jan	100	1972:	April	200
	March	60		Total	200
	April	30			
	May	30	1978:	Nov	2,275
	July	71		Total	2,275
	Aug	282			
	Sept	35			
	Oct	31			
	Nov	12			
	Dec	30			
	Total	681	Grand Total		5,828 1/

1/ Equivalent to about $6.5 billion at exchange rates prevailing at the time of each drawing.

ANNEX C

<u>Budgetary and Accounting Treatment of Transactions with the IMF under the U.S. Quota in the IMF and U.S. Loans to the IMF</u>

Under budget and accounting procedures established in consultations with the Congress at the time of the 1980 increase in the U.S. IMF quota, an increase in the U.S. quota or line of credit to the IMF requires budget authorization and appropriation for the full amount of increases in the quota or U.S. lending arrangements. The sum is included in the budget authority totals for the fiscal year requested. Payment to the IMF of the increased quota subcription is made partly (25 percent) in reserve assets (SDRs or foreign currencies) and partly in non-interest bearing letters of credit, which are a contingent liability. Under the credit lines established pursuant to IMF borrowing arrangements with the United States, the Treasury is committed to provide funds upon call by the IMF.

A budget expenditure occurs only as cash is actually transferred to the IMF, through the 25 percent reserve asset payment, through encashment of the quota letter of credit, or against the borrowing arrangements. Simultaneous with such transfers, the U.S. receives an equal offsetting receipt, representing an increase in the U.S. reserve position in the IMF -- an interest-bearing, liquid international monetary asset that is available unconditionally to the United States in case of balance of payments need. As a consequence of these offsetting transactions, transfers to the IMF under the quota subscription or U.S. lending arrangements therefore do not result in net budget outlays, or directly affect the budget deficit. Similarly, payments of dollars by the IMF to the United States (for example, resulting from repayments by other IMF member countries) do not result in net budget receipts since the U.S. reserve position declines simultaneously by a like amount.

Transfers from the United States to the IMF under the U.S. quota or U.S. lending arrangements increase Treasury borrowing requirements, while transfers from the IMF to the United States improve Treasury's cash position and reduce the borrowing requirement. The net effect of transfers to and from the IMF has varied widely over the years, resulting in cash outflows from the Treasury in some years and inflows to the Treasury in other years. Moreover, Treasury interest costs on borrowings to finance any net transfers to the IMF need to be balanced against the remuneration (interest) earned on the U.S. reserve position in the IMF. Finally, the U.S. may incur exchange gains and losses on the U.S. reserve position in the IMF due to changes in the dollar value of the SDR.

It is not possible to project the effect on Treasury borrowing requirements or the net cost of U.S. transactions with the IMF because of uncertainties regarding the future level of IMF financing; the portion of such financing that would be in dollars; and movements in market interest and exchange rates. However, the figures in the attached table indicate that for the period from May 1, 1969 to the end of 1982:

-- Net increases in Treasury borrowing requirements attributable to transactions with the IMF averaged $454 million annually, compared to average annual increases in Federal borrowing of $54 billion.

-- Treasury debt outstanding attributable to transactions with the IMF averaged $1.6 billion annually. This is not an annual increase in Treasury borrowing, but an estimate of the average total debt outstanding each year attributable to cumulative U.S. transactions with the IMF. As of December 31, 1982, the outstanding borrowing attributable to such transactions amounted to $6.3 billion, about 1/2 of 1 percent of the total outstanding Treasury debt of $1.2 trillion.

-- Net interest costs to the Treasury associated with all U.S. transactions with the IMF averaged $42 million annually. In fiscal 1982, interest costs on total Treasury debt amounted to $117 billion.

-- Net valuation losses to the U.S. on the U.S. reserve position in the IMF averaged $69 million.

-- The overall net annual cost to the U.S., taking account of interest and valuation, thus averaged $111 million.

Estimated Gains and Losses Associated With U.S. Transactions
Under U.S. Quota and U.S. Loans to IMF
(millions of dollars)

Year Ended April 30 1/	Cumulative Net Treasury Debt(-) or Cash(+) Position Arising From: Transactions Under U.S. Quota 2/ (1)	U.S. Loans to IMF 3/ (2)	Total 4/ (3)	Borrowing Cost(-) or Reduction(+) from Column(3) 5/ (4)	Interest Received by U.S. on Loans to IMF 6/ (5)	Remuneration Received by U.S. from IMF 7/ (6)	Valuation Gains(+) or Losses(-) on U.S. Reserve Position 8/ (7)	Interest Earned on Holdings of Foreign Currencies Drawn from IMF 9/ (8)	Total Net Gains(+) or Losses(-) 10/ (9)
1970	-716	-	-716	-50	-	+13	-	-	-37
1971	-702	-	-702	-38	-	+12	-	-	-26
1972	+445	-	+445	+19	-	*	-	-	+19
1973	+811	-	+811	+39	-	-	+34	-	+73
1974	+704	-	+704	+54	-	-	+54	-	+108
1975	-300	-	-300	-22	-	*	+70	-	+48
1976	-940	-	-940	-52	-	+9	-182	-	-225
1977	-2,695	-131	-2,826	-138	+3	+79	+54	-	-2
1978	-2,726	-639	-3,365	-197	+26	+79	+219	-	+127
1979	-1,368	-329	-1,697	-140	+28	+30	+223	+25	+166
1980	-555	-16	-571	-65	-	-	+15	+46	-4
1981	-1,294	-334	-1,628	-192	+16	+22	-203	+63	-294
1982	-3,416	-862	-4,278	-581	+88	+216	-1,134	+75	-1,336
1983 thru 12/31/82	-5,092	-1,216	-6,308	-364	+64	+222	-94	+39	-133
Total Period: 5/1/69-12/31/82	-17,844	-3,527	-21,371	-1,727	+225	+682	-944	+248	-1,516
Annual Average	-1,306	-258	-1,564	-126	+16	+50	-69	+18	-111

Footnotes

*Indicates less than $500,000.

1/ Represents IMF fiscal year.

2/ Includes U.S. transfers of dollars to the IMF (i.e., an outflow of dollars from Treasury) and dollar balances received by the U.S. from the IMF and from sales of foreign currency drawn by the U.S. from the IMF (i.e., an inflow of dollars to the Treasury).

3/ Includes U.S. loans and repayments under the IMF's General Arrangements to Borrow and Supplementary Financing Facility.

4/ Transfers to and from the IMF under the U.S. quota subscription or U.S. lending arrangements result in budget outlays and simultaneous receipts of U.S. reserve position in the IMF; these transactions have a zero effect on net outlays and the budget deficit.

5/ Equals column 3 times average Treasury 3-month bill rate during period. Payments enter the U.S. budget as interest on the public debt; inflows reduce Treasury's need to borrow and thus reduce interest expense.

6/ Enters the U.S. budget as a receipt.

7/ Remuneration on U.S. creditor position; prior to 1975, remuneration was 1.5%, although special income distributions were made in 1970 and 1971 which raised the effective rate to 2.0 percent in those years. From 1975, the rate was based on short-term market interest rates in the five largest IMF members (U.S., U.K., Germany, France, Japan). Enters the U.S. budget as a receipt. Payments are made by IMF annually, as of April 30; FY 1983 figure represents net accrual as of December 31, 1982.

8/ Reflects changes in the dollar value of the U.S. reserve position in the IMF due to an appreciation (-) or depreciation (+) of the dollar in terms of the SDR. Enters the U.S. budget as a positive or negative net outlay.

9/ Interest earned on investments of German marks and Japanese yen acquired from U.S. drawing on IMF in November 1978. Enters the U.S. budget as part of the net profit or loss of the Exchange Stabilization Fund of the Treasury, recorded as a positive or negative net outlay.

10/ Equal to the sum of columns 4 through 8.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. February 15, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $12,400 million, to be issued February 24, 1983. This offering will provide $1,250 million of new cash for the Treasury, as the maturing bills were originally issued in the amount of $ 11,153 million. The two series offered are as follows:

91-day bills (to maturity date) for approximately $6,200 million, representing an additional amount of bills dated November 26, 1982, and to mature May 26, 1983 (CUSIP No. 912794 CV 4), currently outstanding in the amount of $5,622 million, the additional and original bills to be freely interchangeable.

182-day bills for approximately $ 6,200 million, to be dated February 24, 1983, and to mature August 25, 1983 (CUSIP No. 912794 DN 1).

Both series of bills will be issued for cash and in exchange for Treasury bills maturing February 24, 1983. In addition to the maturing 13-week and 26-week bills, there are $5,271 million of maturing 52-week bills. The disposition of this latter amount was announced last week. Federal Reserve Banks, as agents for foreign and international monetary authorities, currently hold $1,566 million, and Federal Reserve Banks for their own account hold $3,133 million of the maturing bills. These amounts represent the combined holdings of such accounts for the three issues of maturing bills.

Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them. For purposes of determining such additional amounts, foreign and international monetary authorities are considered to hold $1,246 million of the original 13-week and 26-week issues.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

R-2030

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Tuesday, February 22, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the easury of the amount and price range of accepted bids. Competive bidders will be advised of the acceptance or rejection of eir tenders. The Secretary of the Treasury expressly reserves e right to accept or reject any or all tenders, in whole or in rt, and the Secretary's action shall be final. Subject to these servations, noncompetitive tenders for each issue for $500,000 less without stated price from any one bidder will be accepted full at the weighted average price (in three decimals) of cepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained the book-entry records of Federal Reserve Banks and Branches st be made or completed at the Federal Reserve Bank or Branch February 24, 1983, in cash or other immediately-available funds in Treasury bills maturing February 24, 1983. Cash adjustments ll be made for differences between the par value of the maturing lls accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the ount of discount at which these bills are sold is considered to crue when the bills are sold, redeemed, or otherwise disposed of. ction 1232(a)(4) provides that any gain on the sale or redempon of these bills that does not exceed the ratable share of the quisition discount must be included in the Federal income tax turn of the owner as ordinary income. The acquisition discount the excess of the stated redemption price over the taxpayer's sis (cost) for the bill. The ratable share of this discount determined by multiplying such discount by a fraction, the merator of which is the number of days the taxpayer held the ll and the denominator of which is the number of days from the y following the taxpayer's date of purchase to the maturity of e bill. If the gain on the sale of a bill exceeds the taxpayer's table portion of the acquisition discount, the excess gain is eated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - s. 26-76 and 27-76, and this notice, prescribe the terms of ese Treasury bills and govern the conditions of their issue. pies of the circulars and tender forms may be obtained from any deral Reserve Bank or Branch, or from the Bureau of the Public bt.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

TREAS

FOR RELEASE UPON DELIVERY
EXPECTED AT 9:30 A.M.
Tuesday, February 15, 1983

TESTIMONY OF THE HONORABLE DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
SENATE APPROPRIATIONS COMMITTEE

Mr. Chairman and Members of the Committee:

It is a pleasure to meet with you today and to discuss the Administration's 1984 budget proposals. The development of a sound fiscal policy was one of the central objectives of the Reagan Administration when it came into office two years ago. For too long a time Americans had watched the share of GNP accounted for by Federal spending and taxes move upward. As the government siphoned off resources from the private sector and the money supply expanded, economic activity stagnated and inflation soared.

In February 1981 the Administration put before Congress a four point plan to revitalize the economy. Our program included spending restraint, tax reductions, regulatory reform, and support of the Federal Reserve's efforts to attain gradual, steady reduction in the rate of monetary growth.

The transition to a noninflationary environment has been somewhat more difficult than anticipated. We have seen two years of serious economic recession as a result of the inflation/tax spiral and monetary volatility.

However, the recession now appears to be over. The unemployment rate declined in January for the first time since July 1981. There has been clear progress on inflation, and consumer price growth has dropped dramatically from 12.4 percent in 1980 to 3.9 percent in 1982. The producer price index fell by 1.0 percent in January -- the sharpest drop in the history of the index. Interest rates, which had been driven to record levels by inflation, are down from peak levels of 21-1/2 percent on the prime in December 1980 to 11 percent

R-2031

currently, and the stock market last year made new highs. Indicators such as housing, inventories, and real income show the economy is poised for recovery. Despite these favorable developments, further reductions in unemployment are still necessary.

The task now is to encourage the renewal of economic growth to reduce unemployment and provide productive job opportunities in the private sector. In so doing we must not repeat the errors of the past and return to an inflationary economy.

The current domestic situation is complicated by the existence of large Federal budget deficits and the threat of even larger ones in years to come. These budget deficits will have to be reduced, since their persistence would inevitably lead to very adverse consequences for the U.S. economy and its financial markets.

Many of the economic difficulties we face at home are also faced by countries abroad. The entire international economy is experiencing a severe slowdown, complicated by the special debt-servicing problems of a number of countries. My prepared statement today deals primarily with the U.S. domestic economy, but it is obvious that the domestic and international situations are closely linked. The clear need in both cases is to encourage expansion rather than undergo further contraction.

It is important to recognize that current difficulties are the culmination of a long period of deteriorating economic performance in this country. The U.S. economy was in deep trouble long before the current recession began. It follows that our policies must aim at lasting long-run solutions. There are no quick cures.

Inflation has led to a roughly parallel rise in key interest rates. As shown in Chart I on interest rates and inflation, the 3-month Treasury bill rate followed the rate of inflation very closely over most of the period from the early 1960's to present. Thus, inflation appears to have been a major factor in the increase in the bill rate during that time.

Rising rates of inflation after the mid-1960's did not lead to more rapid economic growth for any sustained period of time. Quite the contrary. Inflation and its inevitable consequence of higher interest rates finally choked off real growth altogether.

Approach of the Reagan Administration

The Administration's primary economic goal upon coming to office was a fundamental restructuring of the economy, including:

- bringing inflation under control;
- shifting the composition of activity away from government spending toward more productive endeavors in the private sector;
- providing an environment which would reward innovation, work effort, saving and investment, and in which free-market forces could operate effectively.

Over the past two years we have seen evidence that the Administration's program is working. The fundamental elements of recovery are now largely in place. Inflation has been brought under control. Interest rates are coming down, as shown in Chart II. Real wage growth is being restored. In addition, there have been other improvements -- notably in productivity growth and saving behavior -- which mark a shift away from the problems that contributed to sluggish economic performance in recent years.

Within this framework of very significant achievements, there remains the fact that the economy has been in recession and unemployment is still high. The civilian unemployment rate of 10.4 percent in January is, of course, a matter of great concern. The President has indicated in his State of the Union Message that he will be submitting special legislation to help deal with the problem.

The Current State of the Economy

The economy now stands poised for recovery. In fact, the recovery appears to be underway at this moment. It has been much longer in coming than we, or for that matter nearly all forecasters, had expected.

The delay occurred primarily because of the persistence of high interest rates and because of developments in the international sphere. On the international front, the economies of our leading trading partners continued to weaken. Weakness among all the industrialized nations was self-reinforcing. Furthermore, the financial difficulties of some of the newly industrializing nations had adverse impacts on economic activity here. These forces, combined with a general hesitancy on the part of the consumer, led to another round of inventory cutting in the second half of 1982 and delayed the expected turnaround of the economy.

Signals of an Economic Upturn

There are now clear signals that the economy has turned around and that the recession is now behind us. To summarize these signals:

- The unemployment rate for the civilian labor force fell sharply from 10.8 percent in December to 10.4 percent in January.

- The index of leading indicators has risen for eight out of the last nine months.

- Housing is in the midst of a rapid recovery.

- Business trimmed inventories sharply in the final quarter of last year. Historically, a cleanout of inventories typically has been followed by a shift back to higher rates of production.

- Retail sales have begun to firm.

- Total industrial production stabilized in December and evidence available on employment and workhours in January indicates that production will almost certainly rise for the month.

The Typical Recovery

We would all hope for a vigorous recovery, not unlike those which occurred in the past. The typical postwar recovery path is shown in Chart III. Excluded from it are two atypical recoveries -- the first of which included the Korean War buildup and the second which got underway late in 1980 but was short-lived. The five recoveries contained in the average line in the chart were remarkably similar. Gains over the first eight quarters from the real GNP trough were within an extremely narrow range of 5 to 6 percent at an annual rate.

The contributions of GNP components to real growth during the typical recovery are shown in Chart IV. As it indicates, much of the initial thrust for expansion comes from:

- a resurgence in homebuilding activity, such as currently is underway;

- a swing in inventory investment from decumulation in the later stages of recession to accumulation; and

- a major contribution from consumer spending, with purchases of consumer durables registering particularly large increases.

By contrast, Federal spending normally declines as a share of GNP during recovery, and is not necessary for promoting expansion.

<u>The Outlook for the Economy</u>

A vigorous recovery of the type outlined would be most welcome. It would certainly help ease the Nation's budgetary problems. However, we recognize that the serious problems still confronting us may well hold growth during the next year or two below the typical recovery pattern.

- Our overall trade balance is likely to register further marked deterioration in the coming year.

- Real interest rates may persist at high levels, though remaining below those prevailing a year ago.

- The economy is in the process of undergoing marked structural change. Some of our industries may not quickly regain the vitality they experienced in the 1950's and 1960's. The shift of resources to emerging industries will take time.

- Most fundamentally, we are not yet fully out of the inflationary woods, and we cannot afford to direct monetary and fiscal policy toward excessively rapid economic expansion.

For these reasons, the Administration's official forecast contains a fairly conservative estimate of real growth at a 3.1 percent rate during the four quarters of 1983, rather than the typical recovery growth rate of about twice that much. The favorable results in the January employment survey indicate that recovery could well be stronger than forecasted, which we would certainly welcome. Growth is expected to average in the 4 percent range in 1984 and the years beyond.

The Congressional Budget Office forecast for 1983 and 1984 is roughly similar to the Administration's. It also shows moderate growth, well below the average cyclical recovery. Both forecasts are cautious and note uncertainty about the recovery.

However, the CBO is somewhat more optimistic about real GNP growth, unemployment, inflation, and interest rates in 1983 and 1984. The differences are modest in the first year and narrow in the second. According to CBO:

- Real GNP is expected to grow by 4 percent over the four quarters of 1983 and 4.7 percent during 1984 (compared to Administration estimates of 3.1 percent and 4.0 percent).

- Unemployment continues at very high levels, declining only gradually during the recovery, with average unemployment rates of 10.6 and 9.8 percent for the civilian labor force in calendar years 1983 and 1984. The Administration estimates 10.7 percent and 9.9 percent, respectively.

- The GNP deflator rises 4.7 percent in 1983, according to CBO estimates, and 4.6 percent in 1984 (compared to Administration estimates of 5.6 percent and 5.0 percent, respectively).

On balance, the CBO forecast shows somewhat stronger growth from 1983 through 1986, although somewhat lower growth in the following three years.

Policies for the Recovery

In setting policy for the remainder of the 1980's, we must recognize what we must not do. We no longer have the freedom of action to revert back to the overly stimulative monetary and fiscal policies pursued at times in the past, for these would surely lead to a resurgence of inflationary pressures and a new round of rising interest rates. Further, we must not reverse the fundamental tax restructuring put in place in 1981, for this was designed to provide the noninflationary incentives without which the private sector would continue to wither.

Policies for a Changing Economic Structure

For years private sector initiative and dynamic market forces have been stifled by unnecessary Federal regulation. It is important that we carry through with policies of reducing the regulatory burden on private industry. Noteworthy successes have been achieved in this area, particularly in the deregulation of the financial system. For the first time in the postwar period, small investors can count on being able to obtain market rates of return on their savings from banks and thrift institutions.

Further, we recognize that our economy and those of the other industrialized nations are undergoing a period of restructuring. This is an era of rapid technological change, and comparative advantage in the production of many goods and services is shifting from the already developed to the newly developing nations. Those nations which expend all their energies shoring up declining industries and resisting change will find themselves with industrial bases that are obsolete and with declining relative standards of living. Their more foresighted and innovative neighbors will be moving forward and capturing newly opening markets.

Government can ease the painful process of structural change within the economy. We have significant new initiatives in the budget to fight unemployment and we are working with the Congress on additional jobs programs.

Finally, in setting the proper course of policy for the 1980's, we must work closely with the other industrialized and newly industrializing nations of the world. The members of the International Monetary Fund (IMF) have agreed in principle on measures to strengthen the ability of the IMF to deal with current strains in the international financial system. These measures include an increase in IMF quotas of 47.5 percent, from SDR 61 billion (the equivalent of about $67 billion) to SDR 90 billion (about $99 billion), and an expansion of the General Arrangements to Borrow (GAB) from about SDR 6.5 billion ($7 billion) to SDR 17 billion (about $19 billion). The proposed increase in the U.S. quota would be about SDR 5.3 billion, to a new level of SDR 17.9 billion, and our share of the expanded GAB would be SDR 4.25 billion.

The participation of the United States in the increase in IMF resources is an essential complement to domestic measures for economic recovery and represents a valuable investment in defense of the economic interests of the American farmer, laborer, businessman, and consumer. Legislation providing for budget authorization and appropriation for the U.S. share of the increase in IMF resources will be submitted in the near future. The increase in U.S. funding for the IMF, SDR 7.7 billion ($8.5 billion), does not involve net budget outlays or affect the budget deficit because any transfers by the United States to the IMF are simultaneously offset by an increase in our international monetary reserve assets. I urge prompt approval by the Congress.

Monetary Policy

In addition to policies aimed at facilitating structural changes within the economy, we must maintain steady monetary and fiscal policies directed at reinvigorating economic activity. Steady, predictable money supply growth at a noninflationary pace has been, and continues to be, one of the major goals of the Administration's economic program. The Federal Reserve's efforts to achieve that goal have been complicated by a number of factors, such as far-reaching institutional changes in the banking and thrift industries. Nevertheless, the Fed has generally been successful, albeit in a somewhat erratic fashion.

Monetary policy faced a difficult and uncertain situation during much of the last year. Rapid institutional change in the form of new money market instruments blurred the boundaries between the various aggregates and made the achievement of any target rates of growth unusually difficult. There is also some indication that the recession may have led to an increased demand for liquidity and precautionary balances. In 1982, growth in monetary velocity -- the rate at which money is used -- turned negative for the first time in nearly three decades. Under the unusual economic and institutional circumstances of 1982, some temporary offset in the form of above-target rates of monetary growth was probably desirable.

The Federal Reserve's efforts to slow money growth have been accompanied by some volatile short-run swings. Growth in M1 was actually negative on a 13-week basis by mid-summer of last year, and then soared to the double-digit range by the end of the year. This recent acceleration has caused some observers to conclude that the fight against inflationary money growth has been abandoned. That is not true. Both the Administration and the Federal Reserve remain committed to the long-run goal of providing money growth at a noninflationary pace consistent with a steady and sustainable expansion of economic activity.

Fiscal Policy

The objectives of our fiscal policy upon coming to office two years ago were two-fold. First, we believed and still believe it was imperative to correct the disincentives to economic performance that had been built into the tax structure over the years. These disincentives arose in large measure, not by design, but through the interaction of a high rate of inflation with a progressive tax system and historical cost accounting of depreciable assets. Second, it was equally imperative to reverse the seemingly inexorable growth of Federal spending, thereby freeing resources for use in the private sector. In moving to achieve these goals, we faced one major constraint, namely that our defense establishment had been allowed to deteriorate badly, so that our national survival mandated a stepped-up rate of defense spending.

The tax reforms that were put in place were designed primarily to restore an adequate rate of return for investment in plant and equipment and to put a halt to the steady ratchetting upward of marginal tax rates on labor and savings income. The investment incentives were necessary to bring long-depressed rates of business capital investment and productivity growth back up to acceptable standards. For individuals, the tax cuts were needed to protect incentives and purchasing power, and to keep American labor competitive in world markets. For the average taxpayer, they will only result in an actual dollar tax cut in 1983, after allowance for the effects of bracket creep and higher social security taxes. And that 1983 cut and tax indexing will be needed to offset bracket creep and increases in social security taxes scheduled to take effect in the future. These measures will greatly improve the competitive standing of American capital and labor in the world as economic recovery proceeds.

I want to discuss briefly the tax cut enacted in 1981 and address some of the misconceptions about the act, namely that the tax cut was much too large and as a result, it destroyed our revenue base and caused the budget deficits we are facing.

Rather than being too large, the tax cut enacted in 1981 just barely offsets rising tax burden on the economy.

Between fiscal 1981 and 1988, ERTA reduces taxes by $1,138 billion, a substantial amount. But a substantial tax cut is needed to offset the equally substantial tax increases facing the American taxpayers between fiscal 1981 and 1988.

- Last summer's tax bill raises taxes by $281 billion.

- The gasoline tax bill raises taxes by $21 billion.

- Inflation-induced bracket creep raises taxes by $489 billion.

- Previously-scheduled social security taxes raise taxes by $214 billion, and the proposed bipartisan social security rescue plan will raise $56 billion.

The total tax increases amount to $1,061 billion, leaving the taxpayers with net tax cut of only $77 billion between 1981 and 1988.

Rather than destroying the tax base, as many have suggested, the 1981 tax cut merely "returns revenues as a percentage of GNP to approximately the levels that prevailed in the 1960's and 1970's," according to the Congressional Budget Office's recent report on the budget.

Under the Administration budget, taxes as a percent of GNP for fiscal years 1983 to 1986 will average 19.2 percent. This is a level slightly higher than the 18.6 percent average for the 1960's and the 18.9 percent average for the 1970's. It is low only in comparison to the high tax level of the previous Administration, which reached 20.9 percent in fiscal 1981.

And as CBO points out, the tax burden during the 1980's "would have moved well above the all-time record of 21.9 percent of GNP reached in 1944" without the tax cuts.

CBO also reports that due to the tax cut individual income taxes as a percent of taxable personal income will average 12.3 percent for the 1984 to 1988 period. This is a level below the 14.3 percent rate in 1981, the highest level in history, but close to the 12.2 percent average rate for the 1970's.

Without the tax cut, CBO notes, the tax rate would have risen to an "unprecedented" 18.4 percent by 1988. And without indexing, the tax rate would rise to the near-record level of almost 14 percent by 1988.

Repeal of the remainder of the tax cut would strike disproportionately at lower income workers and retirees. Repeal of the third year would cause a 13.9 percent jump in tax liability for those with less than $10,000 in adjusted gross income, a 12 percent jump for those between $20,000 and $30,000, and only a 2.7 percent jump for those with $200,000 and over.

The unfairness of repeal is even more pronounced with indexing. Assuming 4.5 percent inflation, repealing indexing would produce a 9.4 percent jump in tax liability for those with less than $10,000 in adjusted gross income, a 3.2 percent jump for those between $20,000 and $30,000, and a one-half percent jump for those with $200,000 and over. Even worse, these latter increases from repeal of indexing would be repeated each year as long as inflation continues.

Indexing is of relatively greatest importance to lower bracket taxpayers. First, the lower brackets are narrowest in percentage terms, and inflation causes income to rise through the brackets fastest at the bottom. Second, for those in the lower brackets, personal exemptions and the zero bracket are large relative to total income. Indexing keeps these exemptions from losing real value, and keeps inflation from pushing those too poor to owe tax onto the tax rolls. Third, upper income taxpayers may already be in the top tax bracket, with no higher bracket into which to be pushed.

In addition to the significance for individuals of the third year cut and indexing, both of these measures are of critical importance for small businesses. Small businesses tend to be labor intensive, and the Administration's program of reducing marginal tax rates and indexing will help limit wage pressures, enabling American labor to maintain competitiveness with workers overseas. In addition, because over 85 percent of small businesses pay only personal income tax, the Administration's tax program will help directly to safeguard the value of their earnings.

There have been suggestions that proposals to delay retirement COLAs or pay increases should be accompanied by repeal of the third year or indexing to increase fairness, as if these proposals somehow impact different groups. In fact, this would impose an unfair double burden on workers, savers, and pensioners of all income levels who are simultaneously income recipients and taxpayers.

We are asking social security recipients to accept a 6-month delay in their cost-of-living increase, and the taxation of a portion of benefits for upper income retirees to help save the Social Security System. It would be unfair to raise tax rates on their other pension or interest income by repealing the third year, or to subject their fixed retirement incomes to continued bracket creep year after year.

Federal workers are being asked to accept a COLA freeze in FY 1984. Many private sector workers are re-negotiating their labor contracts to strengthen their competitiveness and preserve their jobs. They are also facing higher payroll taxes to help preserve the Social Security System. This is particularly true of self-employed small businessmen, who will pay more on their own salaries and as employers of others. It would unfairly compound their difficulties if the third year were repealed, and recompound them every year thereafter if indexing is removed and income tax rates are made to rise continually.

The only beneficiaries of repeal of the third year and indexing would be here in Washington. As for the country at large, substantial job loss would result as American workers were made less competitive by a higher tax burden, and as savers withdrew from the market as rising tax rates lowered the return on their savings.

We were relatively successful in working with the Congress to achieve our goals of tax reform, but we were less successful in the area of outlay control. A major portion of the savings we had proposed in our original budget did not receive favorable action. This, along with much weaker economic activity than expected, has left us facing the prospect of large deficits even as the economy recovers.

The proposals in the FY-1984 Budget are directed at the crucial task of restoring noninflationary economic growth. This requires the preservation of the investment and work incentives provided by the tax reforms of 1981 and a reduction in the high deficits and interest rates which lie ahead unless corrective action is taken to bring government outlays under control.

The tax reforms already enacted will enable us to make good progress in rebuilding and modernizing America's plant and equipment as the recovery progresses. Incentives are in place to encourage saving and investment and to lower the cost of new machinery and structures. Taxes on American labor are coming down. These reforms will lead to a more productive, more competitive United States. The capital formation program will be financed by higher levels of personal saving, more generous capital consumption allowances, and higher retained earnings as profits recover from the current slump. These elements, plus state and local budget surpluses, form the Nation's savings pool.

Spending reduction will contribute to the recovery, and the recovery will contribute to deficit reduction. The deficit will fall as the economy advances, particularly if the recovery is a vigorous one. A strong recovery with 1-1/3 percent more real growth per year than in our forecast would bring the budget to near balance by 1988, provided we also curb the growth of Federal outlays.

However, if we fail to bring spending under control and if recovery is slow, we will face a deficit problem which is larger and longer-lasting than we can afford. In such case, the deficit could run in the range of 6 to 7 percent of GNP each year through 1988. Our tax reforms were designed to raise the private savings share, but still we would face the possibility of draining off a large part of the pool of savings, leaving less available for new capital formation. Interest rates could remain high, and the recovery could stall.

This Administration is determined that deficits of such magnitudes will not come to pass. We came to office with a program of boosting the rate of capital investment in order to place the economy on a faster growth track, and we will not allow ourselves to be diverted from that goal. We will take whatever measures are necessary to narrow the deficit to acceptable levels.

- Preferably, all of the necessary narrowing of the deficit would come from the outlay side. Total Federal spending represents the amount of resources absorbed by the government at the expense of the private sector. This spending can be financed by both taxes and borrowing, which in either case amounts to a drain on private resources. Only through spending reduction will the credit market find itself in a more favorable position.

- In the event that the combination of economic growth and outlay reductions is not sufficient to narrow the deficit to acceptable levels in the outyears, we are prepared to request additional revenue raising measures in those years. If the Congress chooses not to reduce spending, as we wish, then it is preferable to have the full cost of federal spending programs explicitly identified for the taxpayers who bear the burden of financing government. If additional revenues are needed, this Administration will do its best to structure the tax code in a way that minimizes disincentives for productive effort.

Our Budget Proposals

Spending reduction is crucial. Unfortunately, it has been difficult to achieve because of the built-in momentum of Federal spending programs. Consequently, we are proposing strong medicine. None of us will find it agreeable, but it is critical to the restoration of vitality to our economy. There must be assurance that all will share in spending restraint, just as all of us will share in the benefits of a revitalized recovery. We, like a great many other nations in the world, have tried to live beyond our means. Now we must bring our spending into line with our productive capacity and strengthen the private sector which produces our national wealth.

The deficit reduction program that we propose contains four basic elements.

- The first is a freeze on 1984 outlays to the extent possible. Total outlays should be frozen in real terms in 1984. The 6-month freeze on COLAs, as recommended by the Social Security Commission, is to be extended to other indexed programs. There will be a 1-year freeze on pay and retirement of Federal workers, both civilian and military. Many workers in the private sector have accepted freezes in their pay. Federal workers can also make a sacrifice, which hopefully will serve as an example for sectors of the economy which have not yet recognized the need for moderation in wage demands. As a final item of freeze, outlays for a broad range of nonentitlement programs will be held at 1983 levels.

- The second element of our budgetary program contains measures to control the so-called "uncontrollables." Laws have been so written that Federal payments are automatic to all those declared eligible. We plan a careful review of all such programs, taking special care to protect those truly in need.

- The third element is a cutback of $55 billion in defense outlays from original plans.

- Fourth is a set of proposals involving the revenue side of the budget, described below.

We are projecting receipts for the current year (fiscal year 1983) of $597.5 billion. For fiscal year 1984 we expect receipts to be $659.7 billion. The 1983 figure represents a decline of $20.3 billion from the fiscal year 1982 total of $617.8 billion. This decline, and indeed the absence of an increase in receipts in the range of $50-70 billion, is due primarily to the recession. As I have already explained, our economic projections throughout the remainder of the recovery period are cautious. If real GNP grows at a faster rate than we have projected, then receipts for the current fiscal year, as well as for subsequent years, will be somewhat higher than we are now projecting.

In 1984, as the recovery is well underway, receipts are expected to rise to $659.7 billion, an increase over 1983 of $62.2 billion, representing an annual growth of 10.4 percent. This will occur as profit margins recover and other income shares continue to grow.

For the other years in our forecast period (1985-1988) we project an average annual growth rate of receipts about 10 percent without contingency taxes (and 11 percent per year including contingency taxes), with receipts reaching the $1 trillion mark for the first time in fiscal year 1988. All of these projections assume the legislative proposals included in the President's Fiscal Year 1984 Budget. Receipts under existing legislation will also grow, but at a somewhat lower 9-1/2 percent annual average rate.

The estimates of receipts made by the Congressional Budget Office reflect the higher real economic growth forecast by CBO in 1983 through 1985 and the somewhat lower growth thereafter. Thus far, CBO has published only baseline numbers, analogous to current services estimates without policy changes. As compared to the Administration current services projections, CBO estimates receipts to grow more quickly during the first 3 years of the period and more slowly during the latter three years, because of differences in projected rates of real economic growth. CBO's outlay estimates run below the Administration's throughout the period, mainly because of the difference in the basis for estimating defense spending. Therefore, on balance, CBO projects smaller baseline deficits than the Administration does on a current services basis.

It is noteworthy that under Administration proposals individual income tax receipts will continue to rise over the 1985-1988 period, but only as <u>real</u> income rises. Beginning in 1985, we will no longer collect hidden taxes in the form of bracket creep caused by inflation. Without the indexation provision of ERTA, individuals would pay $6 billion more in taxes during fiscal year 1985 alone, and about $100 billion more during the entire forecast period -- 1985 through 1988.

There has been a gradual upward trend in unified budget receipts as a percent of GNP, shown in the top line of Chart V. As shown in the bottom line of the chart, a major shift in the composition of receipts has been the rising share of social insurance and other payroll taxes to fund social security and other retirement benefits.

There is no proposed omnibus tax bill in the President's budget message. However, there are several separate tax items. Proposed tax legislation in the President's budget can be conveniently grouped under three broad headings: Proposals that improve the income security of Americans, proposals that will improve our ability to produce future output, and, as an insurance policy, a contingency or standby tax, which is intended as a clear signal that we will not permit spending to increase in the outyears unless we pay for it up front.

In the first category, our principal recommendation is for adoption of the bipartisan social security proposals. These proposals, which will increase receipts to the social security funds by $9.8 billion in fiscal year 1984, $11.6 billion in 1985, and $10.6 billion in 1986, are necessary to insure the solvency and security of these trust funds.

The second category, proposals to improve the utilization of our human resources, includes the tuition tax credit, the exclusion of earnings on savings for higher education, the jobs tax credit for hiring the long-term unemployed, and the enterprise zone tax incentives. These will all improve our production capacity, either through increased investments in education or, more directly, by getting our currently underutilized force of experienced workers back to work. As a group, these proposals will reduce taxes $0.5 billion in 1984, $1.2 billion in 1985, and $1.7 billion in 1986.

Finally, the President has proposed a contingency tax plan designed to raise revenues of about 1 percent of GNP in the event that, after Congress has adopted the spending reduction proposals, there is insufficient economic growth to reduce the deficit below 2-1/2 percent of GNP. The contingency tax plan would not go into effect on October 1, 1985, unless the economy is growing on July 1, 1985. The contingency tax plan is an insurance program. It is important to have a plan in place so that the country and the world know that we will not tolerate a string of deficits that would exceed 2-1/2 percent of GNP. Chart VI shows the effect on the deficit that the contingency tax would have if it were implemented. It also shows how the budget picture would be altered by stronger expansion such as some private forecasters expect. The deficit path under high growth reflects the assumption that real GNP increases 1-1/3 percentage points faster than in the official forecast path, starting with FY-1983. Such growth would be in line with the performance from the end of 1960 to late 1966.

The contingency tax plan would contain two elements, each raising about half of the revenues that may be required. One element would be a temporary surcharge of 5 percent on individuals and corporations. The other element would be a temporary excise tax on domestically produced and imported oil designed to raise revenues of about $5 per barrel. The contingency tax alternative shown in the budget raises $146 billion over the

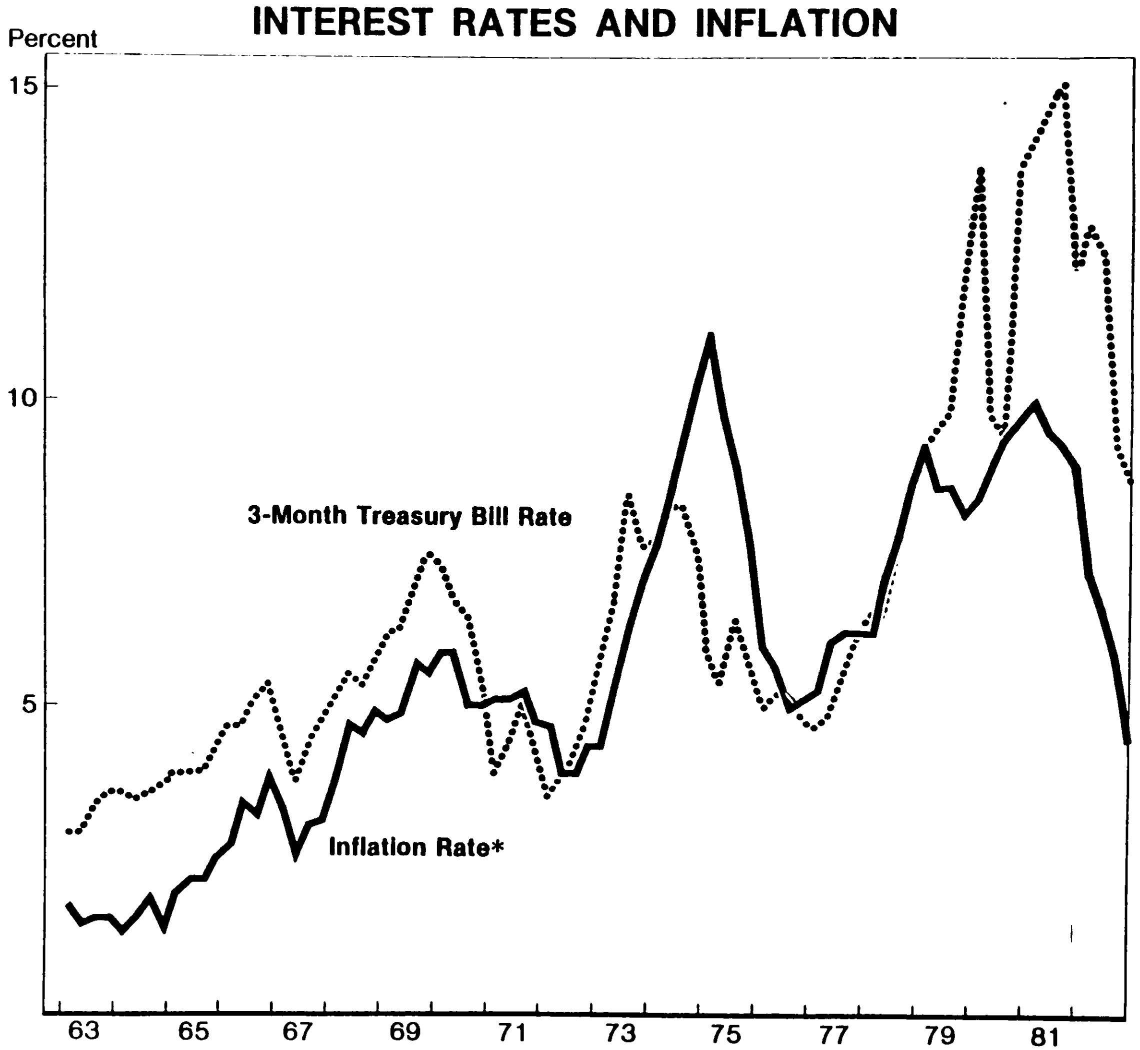
36-month period beginning October 1, 1985. The specific contingency tax plan we will be sending to Congress for adoption this year will be designed to raise revenues of about $130-150 billion over a temporary period of up to 36 months.

If these budget saving proposals are enacted, we will reduce the projected deficits by a total of $580 billion over the next five years, or by $2,400 for every man, woman, and child in the United States. The deficit as a share of GNP will be down to about 2-1/2 percent in 1988 from the 6-1/2 percent we expect this year. Total outlays will grow by only 7 percent per year in nominal terms over the next five years, compared with a bloated 13 percent between 1977 and 1981.

In addition, as part of our overall program, over the next year we will be taking a careful look at the entire structure of our tax system. We will be searching for ways to simplify the tax code and make it fairer while at the same time promoting economic growth by enhancing incentives for work effort, saving, and investment. This is the true road for putting people back to work and bringing the budget into balance.

We are confident that the deficit reduction program contained in this realistic budget is the right program for the economy at this critical juncture. The most important signals we can send the economy are spending restraint, deficit restraint, and a commitment to non-inflationary economic growth throughout the decade. This is the program we have devised. Together with the Congress, we can make it work.

Chart I



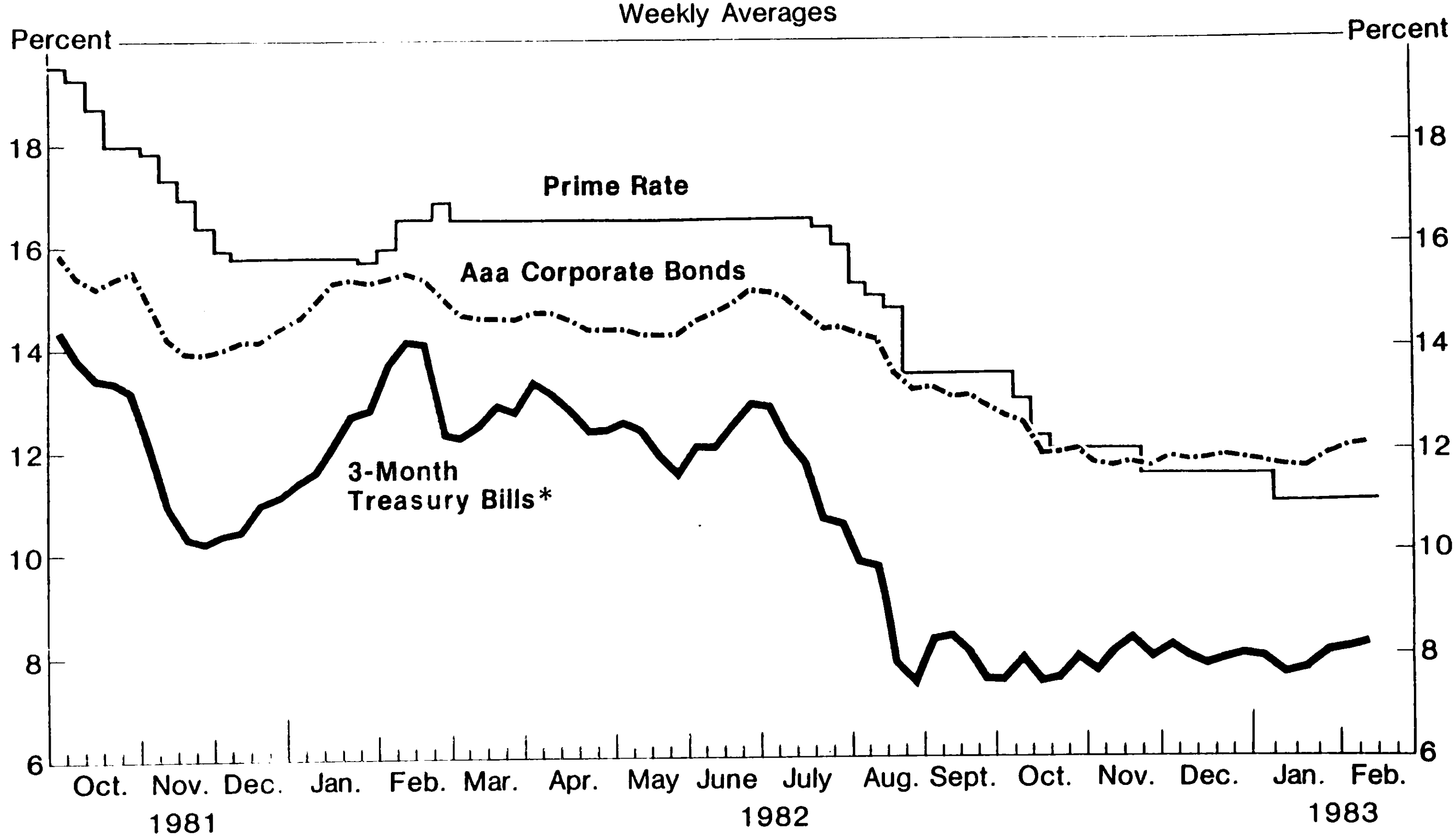
* Growth from year earlier in GNP deflator.
Plotted quarterly.

January 19, 1983-A28

Chart II

INTEREST RATES

Weekly Averages

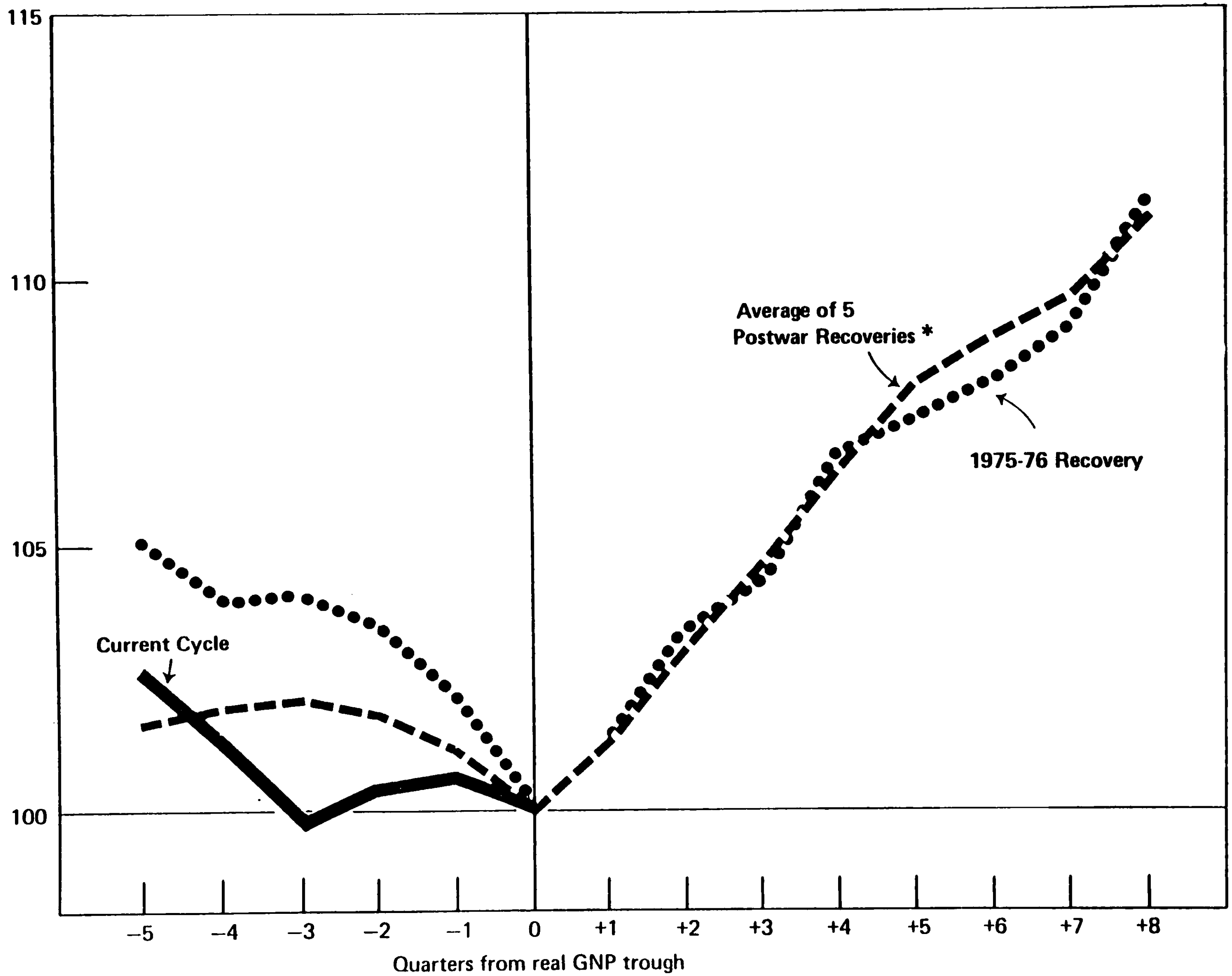


*Bank discount basis

February 14, 1983 A203

THE PATH OF POSTWAR ECONOMIC RECOVERIES

Real GNP trough = 100

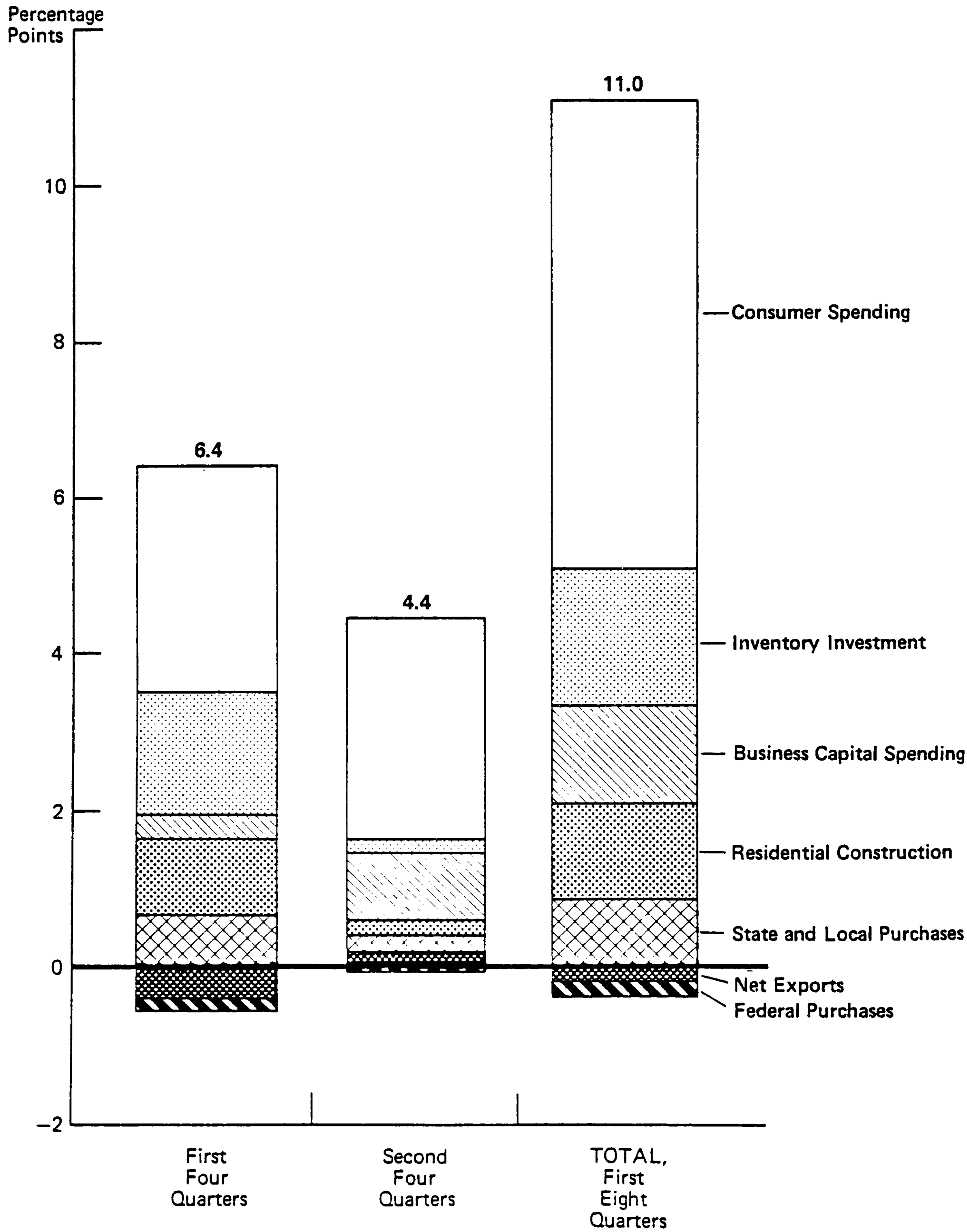


* Postwar recoveries excluding the Korean War period and the short-lived 1980-81 recovery.

January 25, 1983-A210

Chart IV

CONTRIBUTIONS TO A TYPICAL RECOVERY*
BY REAL GNP COMPONENT

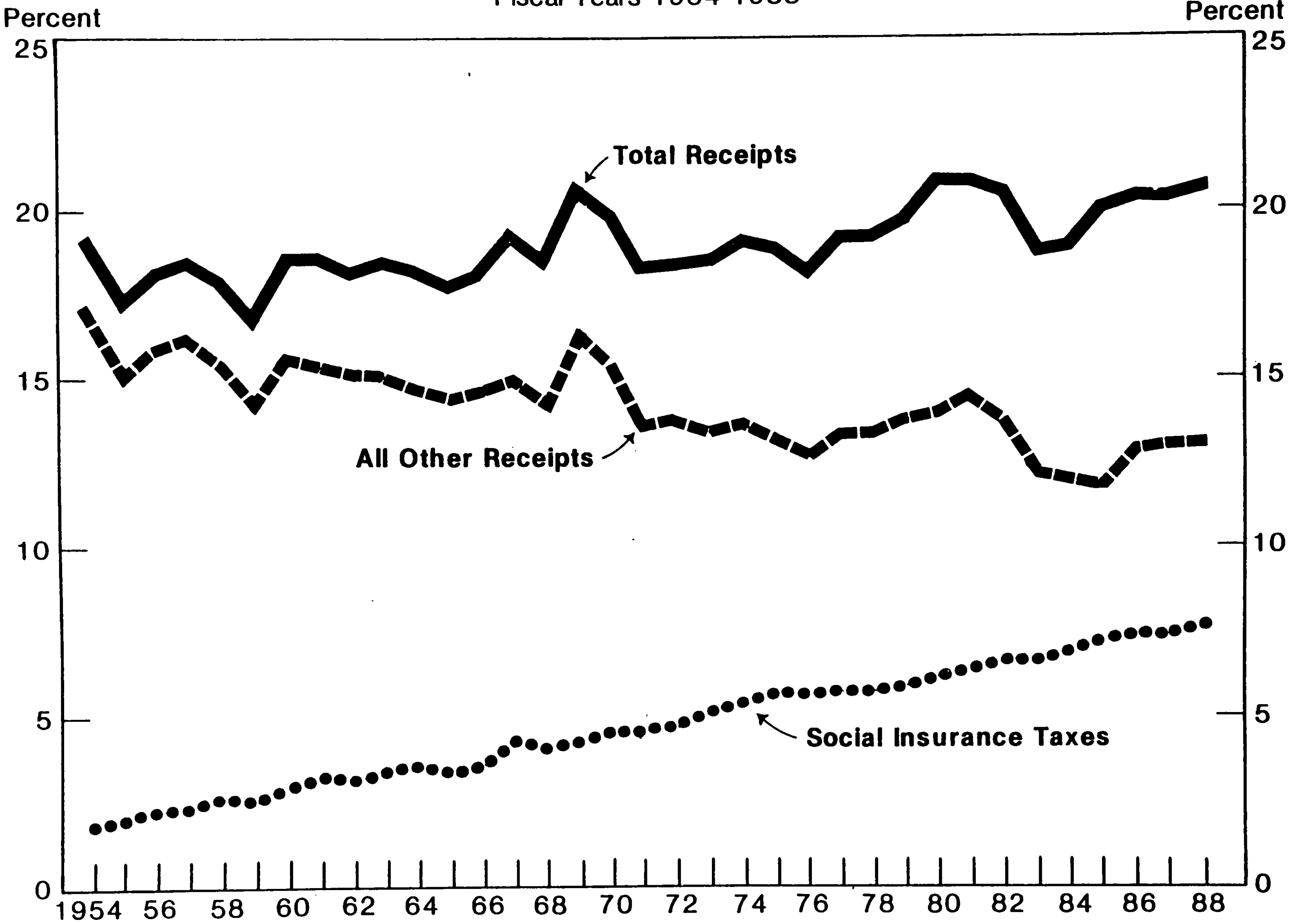


* Average of postwar recoveries, excluding the Korean War period and the short-lived 1980-81 recovery.

January 21, 1983-A213

UNIFIED BUDGET RECEIPTS AS A PERCENT OF GNP *

Fiscal Years 1954-1988

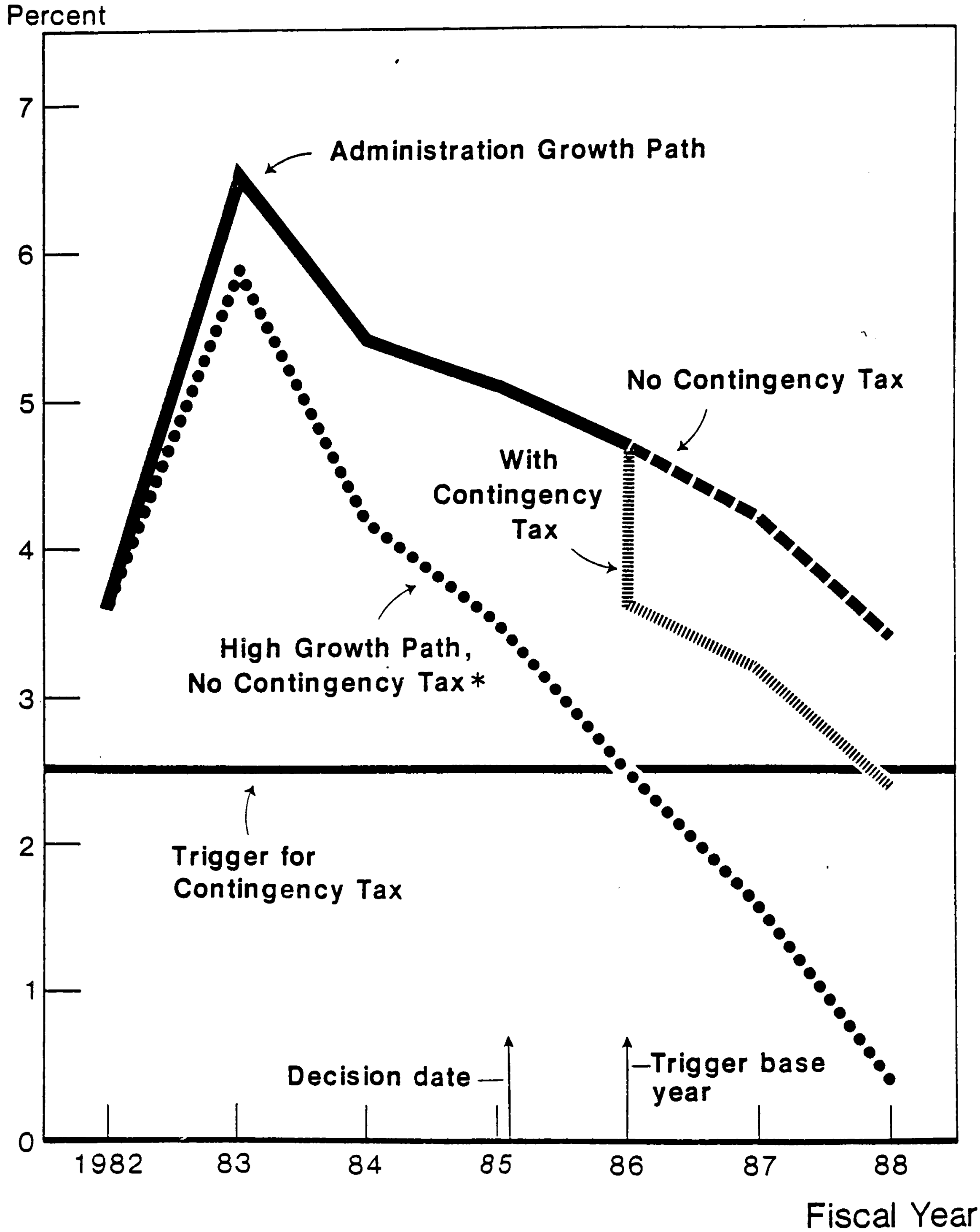


* Receipts include contingency taxes.

January 28, 1983-A215

Chart VI

THE DEFICIT AS A SHARE OF GNP



*Higher growth than the official path by 1-1/3 percentage point starting fiscal year 1983.

January 28, 1983-A214

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TREASURY NEWS

epartment of the Treasury • Washington, D.C. • Telephone 566-2041

TREASURY DEPARTMENT

FOR RELEASE UPON DELIVERY
EXPECTED AT 10:00 A.M.
Wednesday, February 16, 1983

TESTIMONY OF THE HONORABLE DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
SENATE BUDGET COMMITTEE

Mr. Chairman and Members of the Committee:

It is a pleasure to meet with you today and to discuss the Administration's 1984 budget proposals. The development of a sound fiscal policy was one of the central objectives of the Reagan Administration when it came into office two years ago. For too long a time Americans had watched the share of GNP accounted for by Federal spending and taxes move upward. As the government siphoned off resources from the private sector and the money supply expanded, economic activity stagnated and inflation soared.

In February 1981 the Administration put before Congress a four point plan to revitalize the economy. Our program included spending restraint, tax reductions, regulatory reform, and support of the Federal Reserve's efforts to attain gradual, steady reduction in the rate of monetary growth.

The transition to a noninflationary environment has been somewhat more difficult than anticipated. We have seen two years of serious economic recession as a result of the inflation/tax spiral and monetary volatility.

However, the recession now appears to be over. The unemployment rate declined in January for the first time since July 1981. There has been clear progress on inflation, and consumer price growth has dropped dramatically from 12.4 percent in 1980 to 3.9 percent in 1982. The producer price index fell by 1.0 percent in January -- the sharpest drop in the history of the index. Interest rates, which had been driven to record levels by inflation, are down from peak levels of 21-1/2 percent on the prime in December 1980 to 11 percent

R-2032

currently, and the stock market this week made new highs. Indicators such as housing, inventories, and real income show the economy is poised for recovery. Despite these favorable developments, further reductions in unemployment are still necessary.

The task now is to encourage the renewal of economic growth to reduce unemployment and provide productive job opportunities in the private sector. In so doing we must not repeat the errors of the past and return to an inflationary economy.

The current domestic situation is complicated by the existence of large Federal budget deficits and the threat of even larger ones in years to come. These budget deficits will have to be reduced, since their persistence would inevitably lead to very adverse consequences for the U.S. economy and its financial markets.

Many of the economic difficulties we face at home are also faced by countries abroad. The entire international economy is experiencing a severe slowdown, complicated by the special debt-servicing problems of a number of countries. My prepared statement today deals primarily with the U.S. domestic economy, but it is obvious that the domestic and international situations are closely linked. The clear need in both cases is to encourage expansion rather than undergo further contraction.

It is important to recognize that current difficulties are the culmination of a long period of deteriorating economic performance in this country. The U.S. economy was in deep trouble long before the current recession began. It follows that our policies must aim at lasting long-run solutions. There are no quick cures.

Inflation has led to a roughly parallel rise in key interest rates. As shown in Chart I on interest rates and inflation, the 3-month Treasury bill rate followed the rate of inflation very closely over most of the period from the early 1960's to present. Thus, inflation appears to have been a major factor in the increase in the bill rate during that time.

Rising rates of inflation after the mid-1960's did not lead to more rapid economic growth for any sustained period of time. Quite the contrary. Inflation and its inevitable consequence of higher interest rates finally choked off real growth altogether.

Approach of the Reagan Administration

The Administration's primary economic goal upon coming to office was a fundamental restructuring of the economy, including:

- bringing inflation under control;
- shifting the composition of activity away from government spending toward more productive endeavors in the private sector;
- providing an environment which would reward innovation, work effort, saving and investment, and in which free-market forces could operate effectively.

Over the past two years we have seen evidence that the Administration's program is working. The fundamental elements of recovery are now largely in place. Inflation has been brought under control. Interest rates are coming down, as shown in Chart II. Real wage growth is being restored. In addition, there have been other improvements -- notably in productivity growth and saving behavior -- which mark a shift away from the problems that contributed to sluggish economic performance in recent years.

Within this framework of very significant achievements, there remains the fact that the economy has been in recession and unemployment is still high. The civilian unemployment rate of 10.4 percent in January is, of course, a matter of great concern. The President has indicated in his State of the Union Message that he will be submitting special legislation to help deal with the problem.

The Current State of the Economy

The economy now stands poised for recovery. In fact, the recovery appears to be underway at this moment. It has been much longer in coming than we, or for that matter nearly all forecasters, had expected.

The delay occurred primarily because of the persistence of high interest rates and because of developments in the international sphere. On the international front, the economies of our leading trading partners continued to weaken. Weakness among all the industrialized nations was self-reinforcing. Furthermore, the financial difficulties of some of the newly industrializing nations had adverse impacts on economic activity here. These forces, combined with a general hesitancy on the part of the consumer, led to another round of inventory cutting in the second half of 1982 and delayed the expected turnaround of the economy.

Signals of an Economic Upturn

There are now clear signals that the economy has turned around and that the recession is now behind us. To summarize these signals:

- The unemployment rate for the civilian labor force fell sharply from 10.8 percent in December to 10.4 percent in January.
- The index of leading indicators has risen for eight out of the last nine months.
- Housing is in the midst of a rapid recovery.
- Business trimmed inventories sharply in the final quarter of last year. Historically, a cleanout of inventories typically has been followed by a shift back to higher rates of production.
- Retail sales have begun to firm.
- Total industrial production stabilized in December and evidence available on employment and workhours in January indicates that production will almost certainly rise for the month.

The Typical Recovery

We would all hope for a vigorous recovery, not unlike those which occurred in the past. The typical postwar recovery path is shown in Chart III. Excluded from it are two atypical recoveries -- the first of which included the Korean War buildup and the second which got underway late in 1980 but was short-lived. The five recoveries contained in the average line in the chart were remarkably similar. Gains over the first eight quarters from the real GNP trough were within an extremely narrow range of 5 to 6 percent at an annual rate.

The contributions of GNP components to real growth during the typical recovery are shown in Chart IV. As it indicates, much of the initial thrust for expansion comes from:

- a resurgence in homebuilding activity, such as currently is underway;
- a swing in inventory investment from decumulation in the later stages of recession to accumulation; and

- a major contribution from consumer spending, with purchases of consumer durables registering particularly large increases.

By contrast, Federal spending normally declines as a share of GNP during recovery, and is not necessary for promoting expansion.

The Outlook for the Economy

A vigorous recovery of the type outlined would be most welcome. It would certainly help ease the Nation's budgetary problems. However, we recognize that the serious problems still confronting us may well hold growth during the next year or two below the typical recovery pattern.

- Our overall trade balance is likely to register further marked deterioration in the coming year.

- Real interest rates may persist at high levels, though remaining below those prevailing a year ago.

- The economy is in the process of undergoing marked structural change. Some of our industries may not quickly regain the vitality they experienced in the 1950's and 1960's. The shift of resources to emerging industries will take time.

- Most fundamentally, we are not yet fully out of the inflationary woods, and we cannot afford to direct monetary and fiscal policy toward excessively rapid economic expansion.

For these reasons, the Administration's official forecast contains a fairly conservative estimate of real growth at a 3.1 percent rate during the four quarters of 1983, rather than the typical recovery growth rate of about twice that much. The favorable results in the January employment survey indicate that recovery could well be stronger than forecasted, which we would certainly welcome. Growth is expected to average in the 4 percent range in 1984 and the years beyond.

The Congressional Budget Office forecast for 1983 and 1984 is roughly similar to the Administration's. It also shows moderate growth, well below the average cyclical recovery. Both forecasts are cautious and note uncertainty about the recovery.

However, the CBO is somewhat more optimistic about real GNP growth, unemployment, inflation, and interest rates in 1983 and 1984. The differences are modest in the first year and narrow in the second. According to CBO:

- Real GNP is expected to grow by 4 percent over the four quarters of 1983 and 4.7 percent during 1984 (compared to Administration estimates of 3.1 percent and 4.0 percent).

- Unemployment continues at very high levels, declining only gradually during the recovery, with average unemployment rates of 10.6 and 9.8 percent for the civilian labor force in calendar years 1983 and 1984. The Administration estimates 10.7 percent and 9.9 percent, respectively.

- The GNP deflator rises 4.7 percent in 1983, according to CBO estimates, and 4.6 percent in 1984 (compared to Administration estimates of 5.6 percent and 5.0 percent, respectively).

On balance, the CBO forecast shows somewhat stronger growth from 1983 through 1986, although somewhat lower growth in the following three years.

Policies for the Recovery

In setting policy for the remainder of the 1980's, we must recognize what we must not do. We no longer have the freedom of action to revert back to the overly stimulative monetary and fiscal policies pursued at times in the past, for these would surely lead to a resurgence of inflationary pressures and a new round of rising interest rates. Further, we must not reverse the fundamental tax restructuring put in place in 1981, for this was designed to provide the noninflationary incentives without which the private sector would continue to wither.

Policies for a Changing Economic Structure

For years private sector initiative and dynamic market forces have been stifled by unnecessary Federal regulation. It is important that we carry through with policies of reducing the regulatory burden on private industry. Noteworthy successes have been achieved in this area, particularly in the deregulation of the financial system. For the first time in the postwar period, small investors can count on being able to obtain market rates of return on their savings from banks and thrift institutions.

Further, we recognize that our economy and those of the other industrialized nations are undergoing a period of restructuring. This is an era of rapid technological change, and comparative advantage in the production of many goods and services is shifting from the already developed to the newly developing nations. Those nations which expend all their energies shoring up declining industries and resisting change will find themselves with industrial bases that are obsolete and with declining relative standards of living. Their more foresighted and innovative neighbors will be moving forward and capturing newly opening markets.

Government can ease the painful process of structural change within the economy. We have significant new initiatives in the budget to fight unemployment and we are working with the Congress on additional jobs programs.

Finally, in setting the proper course of policy for the 1980's, we must work closely with the other industrialized and newly industrializing nations of the world. The members of the International Monetary Fund (IMF) have agreed in principle on measures to strengthen the ability of the IMF to deal with current strains in the international financial system. These measures include an increase in IMF quotas of 47.5 percent, from SDR 61 billion (the equivalent of about $67 billion) to SDR 90 billion (about $99 billion), and an expansion of the General Arrangements to Borrow (GAB) from about SDR 6.5 billion ($7 billion) to SDR 17 billion (about $19 billion). The proposed increase in the U.S. quota would be about SDR 5.3 billion, to a new level of SDR 17.9 billion, and our share of the expanded GAB would be SDR 4.25 billion.

The participation of the United States in the increase in IMF resources is an essential complement to domestic measures for economic recovery and represents a valuable investment in defense of the economic interests of the American farmer, laborer, businessman, and consumer. Legislation providing for budget authorization and appropriation for the U.S. share of the increase in IMF resources will be submitted in the near future. The increase in U.S. funding for the IMF, SDR 7.7 billion ($8.5 billion), does not involve net budget outlays or affect the budget deficit because any transfers by the United States to the IMF are simultaneously offset by an increase in our international monetary reserve assets. I urge prompt approval by the Congress.

Monetary Policy

In addition to policies aimed at facilitating structural changes within the economy, we must maintain steady monetary and fiscal policies directed at reinvigorating economic activity. Steady, predictable money supply growth at a noninflationary pace has been, and continues to be, one of the major goals of the Administration's economic program. The Federal Reserve's efforts to achieve that goal have been complicated by a number of factors, such as far-reaching institutional changes in the banking and thrift industries. Nevertheless, the Fed has generally been successful, albeit in a somewhat erratic fashion.

Monetary policy faced a difficult and uncertain situation during much of the last year. Rapid institutional change in the form of new money market instruments blurred the boundaries between the various aggregates and made the achievement of any target rates of growth unusually difficult. There is also some indication that the recession may have led to an increased demand for liquidity and precautionary balances. In 1982, growth in monetary velocity -- the rate at which money is used -- turned negative for the first time in nearly three decades. Under the unusual economic and institutional circumstances of 1982, some temporary offset in the form of above-target rates of monetary growth was probably desirable.

The Federal Reserve's efforts to slow money growth have been accompanied by some volatile short-run swings. Growth in M1 was actually negative on a 13-week basis by mid-summer of last year, and then soared to the double-digit range by the end of the year. This recent acceleration has caused some observers to conclude that the fight against inflationary money growth has been abandoned. That is not true. Both the Administration and the Federal Reserve remain committed to the long-run goal of providing money growth at a noninflationary pace consistent with a steady and sustainable expansion of economic activity.

Fiscal Policy

The objectives of our fiscal policy upon coming to office two years ago were two-fold. First, we believed and still believe it was imperative to correct the disincentives to economic performance that had been built into the tax structure over the years. These disincentives arose in large measure, not by design, but through the interaction of a high rate of inflation with a progressive tax system and historical cost accounting of depreciable assets. Second, it was equally imperative to reverse the seemingly inexorable growth of Federal spending, thereby freeing resources for use in the private sector. In moving to achieve these goals, we faced one major constraint, namely that our defense establishment had been allowed to deteriorate badly, so that our national survival mandated a stepped-up rate of defense spending.

The tax reforms that were put in place were designed primarily to restore an adequate rate of return for investment in plant and equipment and to put a halt to the steady ratcheting upward of marginal tax rates on labor and savings income. The investment incentives were necessary to bring long-depressed rates of business capital investment and productivity growth back up to acceptable standards. For individuals, the tax cuts were needed to protect incentives and purchasing power, and to keep American labor competitive in world markets. For the average taxpayer, they will only result in an actual dollar tax cut in 1983, after allowance for the effects of bracket creep and higher social security taxes. And that 1983 cut and tax indexing will be needed to offset bracket creep and increases in social security taxes scheduled to take effect in the future. These measures will greatly improve the competitive standing of American capital and labor in the world as economic recovery proceeds.

I want to discuss briefly the tax cut enacted in 1981 and address some of the misconceptions about the act, namely that the tax cut was much too large and as a result, it destroyed our revenue base and caused the budget deficits we are facing.

Rather than being too large, the tax cut enacted in 1981 just barely offsets rising tax burden on the economy.

Between fiscal 1981 and 1988, ERTA reduces taxes by $1,138 billion, a substantial amount. But a substantial tax cut is needed to offset the equally substantial tax increases facing the American taxpayers between fiscal 1981 and 1988.

- Last summer's tax bill raises taxes by $281 billion.
- The gasoline tax bill raises taxes by $21 billion.
- Inflation-induced bracket creep raises taxes by $489 billion.
- Previously-scheduled social security taxes raise taxes by $214 billion, and the proposed bipartisan social security rescue plan will raise $56 billion.

The total tax increases amount to $1,061 billion, leaving the taxpayers with net tax cut of only $77 billion between 1981 and 1988.

Rather than destroying the tax base, as many have suggested, the 1981 tax cut merely "returns revenues as a percentage of GNP to approximately the levels that prevailed in the 1960's and 1970's," according to the Congressional Budget Office's recent report on the budget.

Under the Administration budget, taxes as a percent of GNP for fiscal years 1983 to 1986 will average 19.2 percent. This is a level slightly higher than the 18.6 percent average for the 1960's and the 18.9 percent average for the 1970's. It is low only in comparison to the high tax level of the previous Administration, which reached 20.9 percent in fiscal 1981.

And as CBO points out, the tax burden during the 1980's "would have moved well above the all-time record of 21.9 percent of GNP reached in 1944" without the tax cuts.

CBO also reports that due to the tax cut individual income taxes as a percent of taxable personal income will average 12.3 percent for the 1984 to 1988 period. This is a level below the 14.3 percent rate in 1981, the highest level in history, but close to the 12.2 percent average rate for the 1970's.

Without the tax cut, CBO notes, the tax rate would have risen to an "unprecedented" 18.4 percent by 1988. And without indexing, the tax rate would rise to the near-record level of almost 14 percent by 1988.

Repeal of the remainder of the tax cut would strike disproportionately at lower income workers and retirees. Repeal of the third year would cause a 13.9 percent jump in tax liability for those with less than $10,000 in adjusted gross income, a 12 percent jump for those between $20,000 and $30,000, and only a 2.7 percent jump for those with $200,000 and over.

The unfairness of repeal is even more pronounced with indexing. Assuming 4.5 percent inflation, repealing indexing would produce a 9.4 percent jump in tax liability for those with less than $10,000 in adjusted gross income, a 3.2 percent jump for those between $20,000 and $30,000, and a one-half percent jump for those with $200,000 and over. Even worse, these latter increases from repeal of indexing would be repeated each year as long as inflation continues.

Indexing is of relatively greatest importance to lower bracket taxpayers. First, the lower brackets are narrowest in percentage terms, and inflation causes income to rise through the brackets fastest at the bottom. Second, for those in the lower brackets, personal exemptions and the zero bracket are large relative to total income. Indexing keeps these exemptions from losing real value, and keeps inflation from pushing those too poor to owe tax onto the tax rolls. Third, upper income taxpayers may already be in the top tax bracket, with no higher bracket into which to be pushed.

In addition to the significance for individuals of the third year cut and indexing, both of these measures are of critical importance for small businesses. Small businesses tend to be labor intensive, and the Administration's program of reducing marginal tax rates and indexing will help limit wage pressures, enabling American labor to maintain competitiveness with workers overseas. In addition, because over 85 percent of small businesses pay only personal income tax, the Administration's tax program will help directly to safeguard the value of their earnings.

There have been suggestions that proposals to delay retirement COLAs or pay increases should be accompanied by repeal of the third year or indexing to increase fairness, as if these proposals somehow impact different groups. In fact, this would impose an unfair double burden on workers, savers, and pensioners of all income levels who are simultaneously income recipients and taxpayers.

We are asking social security recipients to accept a 6-month delay in their cost-of-living increase, and the taxation of a portion of benefits for upper income retirees to help save the Social Security System. It would be unfair to raise tax rates on their other pension or interest income by repealing the third year, or to subject their fixed retirement incomes to continued bracket creep year after year.

Federal workers are being asked to accept a COLA freeze in FY 1984. Many private sector workers are re-negotiating their labor contracts to strengthen their competitiveness and preserve their jobs. They are also facing higher payroll taxes to help preserve the Social Security System. This is particularly true of self-employed small businessmen, who will pay more on their own salaries and as employers of others. It would unfairly compound their difficulties if the third year were repealed, and recompound them every year thereafter if indexing is removed and income tax rates are made to rise continually.

The only beneficiaries of repeal of the third year and indexing would be here in Washington. As for the country at large, substantial job loss would result as American workers were made less competitive by a higher tax burden, and as savers withdrew from the market as rising tax rates lowered the return on their savings.

We were relatively successful in working with the Congress to achieve our goals of tax reform, but we were less successful in the area of outlay control. A major portion of the savings we had proposed in our original budget did not receive favorable action. This, along with much weaker economic activity than expected, has left us facing the prospect of large deficits even as the economy recovers.

The proposals in the FY-1984 Budget are directed at the crucial task of restoring noninflationary economic growth. This requires the preservation of the investment and work incentives provided by the tax reforms of 1981 and a reduction in the high deficits and interest rates which lie ahead unless corrective action is taken to bring government outlays under control.

The tax reforms already enacted will enable us to make good progress in rebuilding and modernizing America's plant and equipment as the recovery progresses. Incentives are in place to encourage saving and investment and to lower the cost of new machinery and structures. Taxes on American labor are coming down. These reforms will lead to a more productive, more competitive United States. The capital formation program will be financed by higher levels of personal saving, more generous capital consumption allowances, and higher retained earnings as profits recover from the current slump. These elements, plus state and local budget surpluses, form the Nation's savings pool.

Spending reduction will contribute to the recovery, and the recovery will contribute to deficit reduction. The deficit will fall as the economy advances, particularly if the recovery is a vigorous one. A strong recovery with 1-1/3 percent more real growth per year than in our forecast would bring the budget to near balance by 1988, provided we also curb the growth of Federal outlays.

However, if we fail to bring spending under control and if recovery is slow, we will face a deficit problem which is larger and longer-lasting than we can afford. In such case, the deficit could run in the range of 6 to 7 percent of GNP each year through 1988. Our tax reforms were designed to raise the private savings share, but still we would face the possibility of draining off a large part of the pool of savings, leaving less available for new capital formation. Interest rates could remain high, and the recovery could stall.

This Administration is determined that deficits of such magnitudes will not come to pass. We came to office with a program of boosting the rate of capital investment in order to place the economy on a faster growth track, and we will not allow ourselves to be diverted from that goal. We will take whatever measures are necessary to narrow the deficit to acceptable levels.

- Preferably, all of the necessary narrowing of the deficit would come from the outlay side. Total Federal spending represents the amount of resources absorbed by the government at the expense of the private sector. This spending can be financed by both taxes and borrowing, which in either case amounts to a drain on private resources. Only through spending reduction will the credit market find itself in a more favorable position.

- In the event that the combination of economic growth and outlay reductions is not sufficient to narrow the deficit to acceptable levels in the outyears, we are prepared to request additional revenue raising measures in those years. If the Congress chooses not to reduce spending, as we wish, then it is preferable to have the full cost of federal spending programs explicitly identified for the taxpayers who bear the burden of financing government. If additional revenues are needed, this Administration will do its best to structure the tax code in a way that minimizes disincentives for productive effort.

Our Budget Proposals

Spending reduction is crucial. Unfortunately, it has been difficult to achieve because of the built-in momentum of Federal spending programs. Consequently, we are proposing strong medicine. None of us will find it agreeable, but it is critical to the restoration of vitality to our economy. There must be assurance that all will share in spending restraint, just as all of us will share in the benefits of a revitalized recovery. We, like a great many other nations in the world, have tried to live beyond our means. Now we must bring our spending into line with our productive capacity and strengthen the private sector which produces our national wealth.

The deficit reduction program that we propose contains four basic elements.

- The first is a freeze on 1984 outlays to the extent possible. Total outlays should be frozen in real terms in 1984. The 6-month freeze on COLAs, as recommended by the Social Security Commission, is to be extended to other indexed programs. There will be a 1-year freeze on pay and retirement of Federal workers, both civilian and military. Many workers in the private sector have accepted freezes in their pay. Federal workers can also make a sacrifice, which hopefully will serve as an example for sectors of the economy which have not yet recognized the need for moderation in wage demands. As a final item of freeze, outlays for a broad range of nonentitlement programs will be held at 1983 levels.

- The second element of our budgetary program contains measures to control the so-called "uncontrollables." Laws have been so written that Federal payments are automatic to all those declared eligible. We plan a careful review of all such programs, taking special care to protect those truly in need.

- The third element is a cutback of $55 billion in defense outlays from original plans.

- Fourth is a set of proposals involving the revenue side of the budget, described below.

We are projecting receipts for the current year (fiscal year 1983) of $597.5 billion. For fiscal year 1984 we expect receipts to be $659.7 billion. The 1983 figure represents a decline of $20.3 billion from the fiscal year 1982 total of $617.8 billion. This decline, and indeed the absence of an increase in receipts in the range of $50-70 billion, is due primarily to the recession. As I have already explained, our economic projections throughout the remainder of the recovery period are cautious. If real GNP grows at a faster rate than we have projected, then receipts for the current fiscal year, as well as for subsequent years, will be somewhat higher than we are now projecting.

In 1984, as the recovery is well underway, receipts are expected to rise to $659.7 billion, an increase over 1983 of $62.2 billion, representing an annual growth of 10.4 percent. This will occur as profit margins recover and other income shares continue to grow.

For the other years in our forecast period (1985-1988) we project an average annual growth rate of receipts about 10 percent without contingency taxes (and 11 percent per year including contingency taxes), with receipts reaching the $1 trillion mark for the first time in fiscal year 1988. All of these projections assume the legislative proposals included in the President's Fiscal Year 1984 Budget. Receipts under existing legislation will also grow, but at a somewhat lower 9-1/2 percent annual average rate.

The estimates of receipts made by the Congressional Budget Office reflect the higher real economic growth forecast by CBO in 1983 through 1985 and the somewhat lower growth thereafter. Thus far, CBO has published only baseline numbers, analogous to current services estimates without policy changes. As compared to the Administration current services projections, CBO estimates receipts to grow more quickly during the first 3 years of the period and more slowly during the latter three years, because of differences in projected rates of real economic growth. CBO's outlay estimates run below the Administration's throughout the period, mainly because of the difference in the basis for estimating defense spending. Therefore, on balance, CBO projects smaller baseline deficits than the Administration does on a current services basis.

It is noteworthy that under Administration proposals individual income tax receipts will continue to rise over the 1985-1988 period, but only as <u>real</u> income rises. Beginning in 1985, we will no longer collect hidden taxes in the form of bracket creep caused by inflation. Without the indexation provision of ERTA, individuals would pay $6 billion more in taxes during fiscal year 1985 alone, and about $100 billion more during the entire forecast period -- 1985 through 1988.

There has been a gradual upward trend in unified budget receipts as a percent of GNP, shown in the top line of Chart V. As shown in the bottom line of the chart, a major shift in the composition of receipts has been the rising share of social insurance and other payroll taxes to fund social security and other retirement benefits.

There is no proposed omnibus tax bill in the President's budget message. However, there are several separate tax items. Proposed tax legislation in the President's budget can be conveniently grouped under three broad headings: Proposals that improve the income security of Americans, proposals that will improve our ability to produce future output, and, as an insurance policy, a contingency or standby tax, which is intended as a clear signal that we will not permit spending to increase in the outyears unless we pay for it up front.

In the first category, our principal recommendation is for adoption of the bipartisan social security proposals. These proposals, which will increase receipts to the social security funds by $9.8 billion in fiscal year 1984, $11.6 billion in 1985, and $10.6 billion in 1986, are necessary to insure the solvency and security of these trust funds.

The second category, proposals to improve the utilization of our human resources, includes the tuition tax credit, the exclusion of earnings on savings for higher education, the jobs tax credit for hiring the long-term unemployed, and the enterprise zone tax incentives. These will all improve our production capacity, either through increased investments in education or, more directly, by getting our currently underutilized force of experienced workers back to work. As a group, these proposals will reduce taxes $0.5 billion in 1984, $1.2 billion in 1985, and $1.7 billion in 1986.

Finally, the President has proposed a contingency tax plan designed to raise revenues of about 1 percent of GNP in the event that, after Congress has adopted the spending reduction proposals, there is insufficient economic growth to reduce the deficit below 2-1/2 percent of GNP. The contingency tax plan would not go into effect on October 1, 1985, unless the economy is growing on July 1, 1985. The contingency tax plan is an insurance program. It is important to have a plan in place so that the country and the world know that we will not tolerate a string of deficits that would exceed 2-1/2 percent of GNP. Chart VI shows the effect on the deficit that the contingency tax would have if it were implemented. It also shows how the budget picture would be altered by stronger expansion such as some private forecasters expect. The deficit path under high growth reflects the assumption that real GNP increases 1-1/3 percentage points faster than in the official forecast path, starting with FY-1983. Such growth would be in line with the performance from the end of 1960 to late 1966.

The contingency tax plan would contain two elements, each raising about half of the revenues that may be required. One element would be a temporary surcharge of 5 percent on individuals and corporations. The other element would be a temporary excise tax on domestically produced and imported oil designed to raise revenues of about $5 per barrel. The contingency tax alternative shown in the budget raises $146 billion over the

36-month period beginning October 1, 1985. The specific contingency tax plan we will be sending to Congress for adoption this year will be designed to raise revenues of about $130-150 billion over a temporary period of up to 36 months.

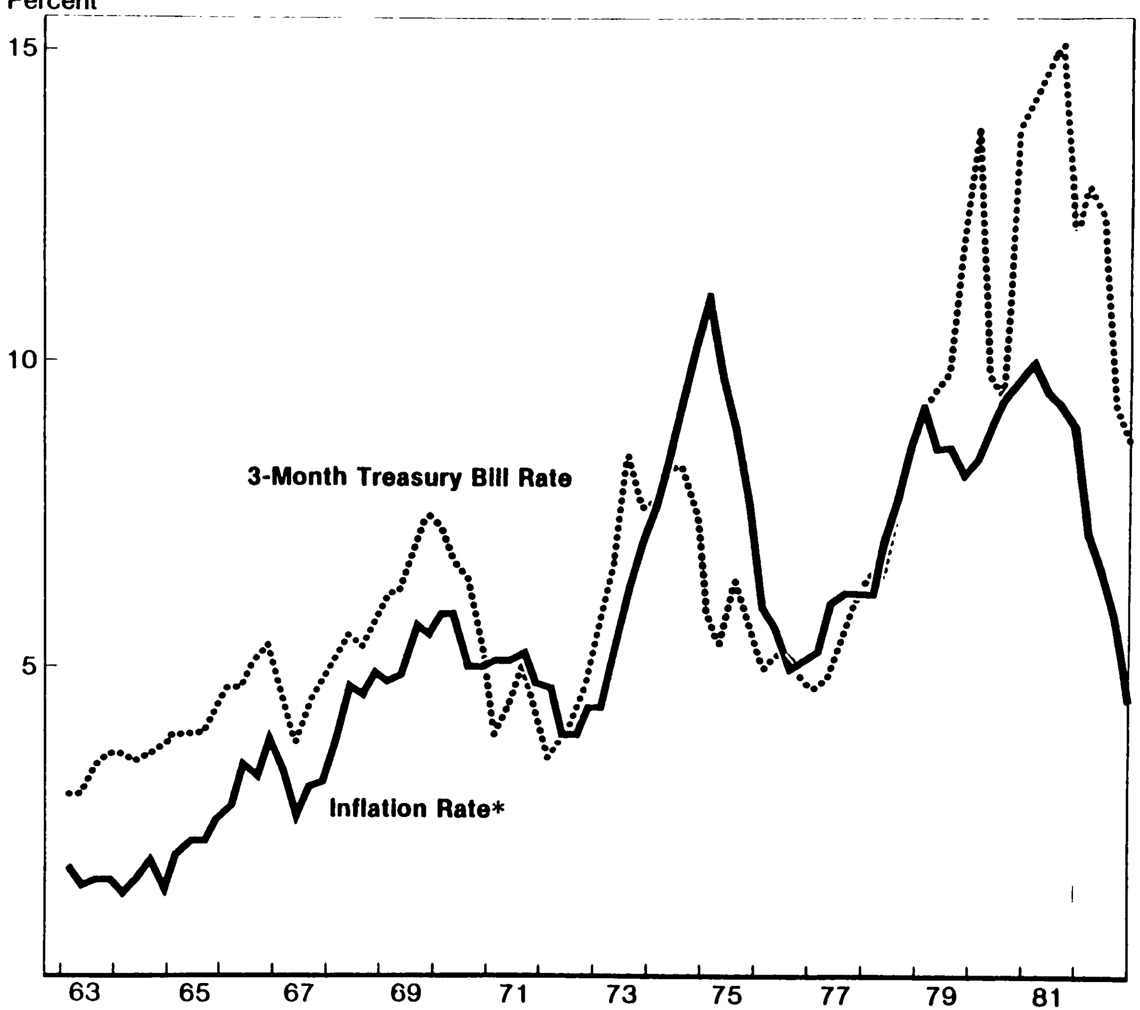
If these budget saving proposals are enacted, we will reduce the projected deficits by a total of $580 billion over the next five years, or by $2,400 for every man, woman, and child in the United States. The deficit as a share of GNP will be down to about 2-1/2 percent in 1988 from the 6-1/2 percent we expect this year. Total outlays will grow by only 7 percent per year in nominal terms over the next five years, compared with a bloated 13 percent between 1977 and 1981.

In addition, as part of our overall program, over the next year we will be taking a careful look at the entire structure of our tax system. We will be searching for ways to simplify the tax code and make it fairer while at the same time promoting economic growth by enhancing incentives for work effort, saving, and investment. This is the true road for putting people back to work and bringing the budget into balance.

We are confident that the deficit reduction program contained in this realistic budget is the right program for the economy at this critical juncture. The most important signals we can send the economy are spending restraint, deficit restraint, and a commitment to non-inflationary economic growth throughout the decade. This is the program we have devised. Together with the Congress, we can make it work.

Chart I

INTEREST RATES AND INFLATION



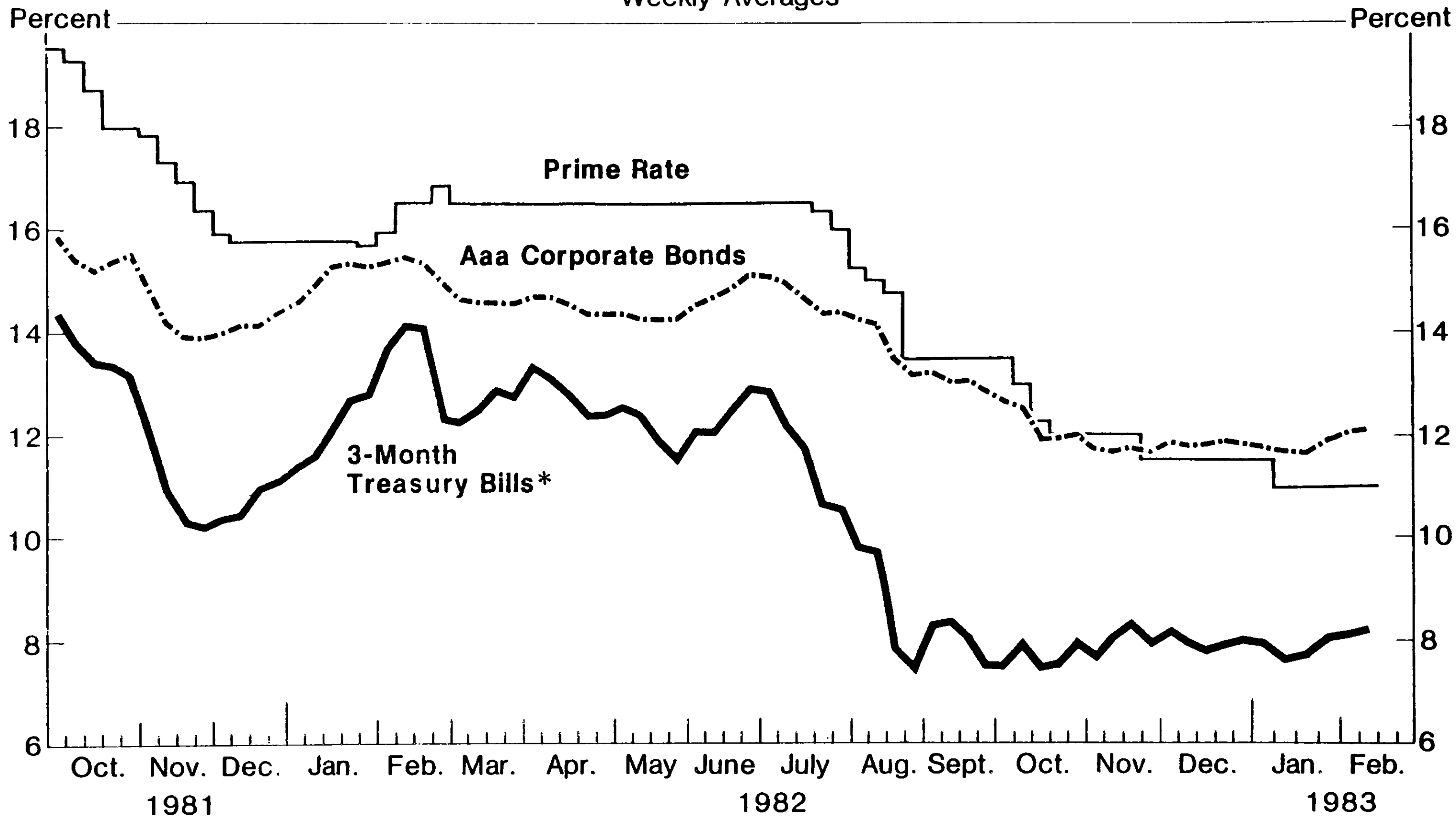
* Growth from year earlier in GNP deflator.
Plotted quarterly.

January 19, 1983 A28

Chart II

INTEREST RATES

Weekly Averages

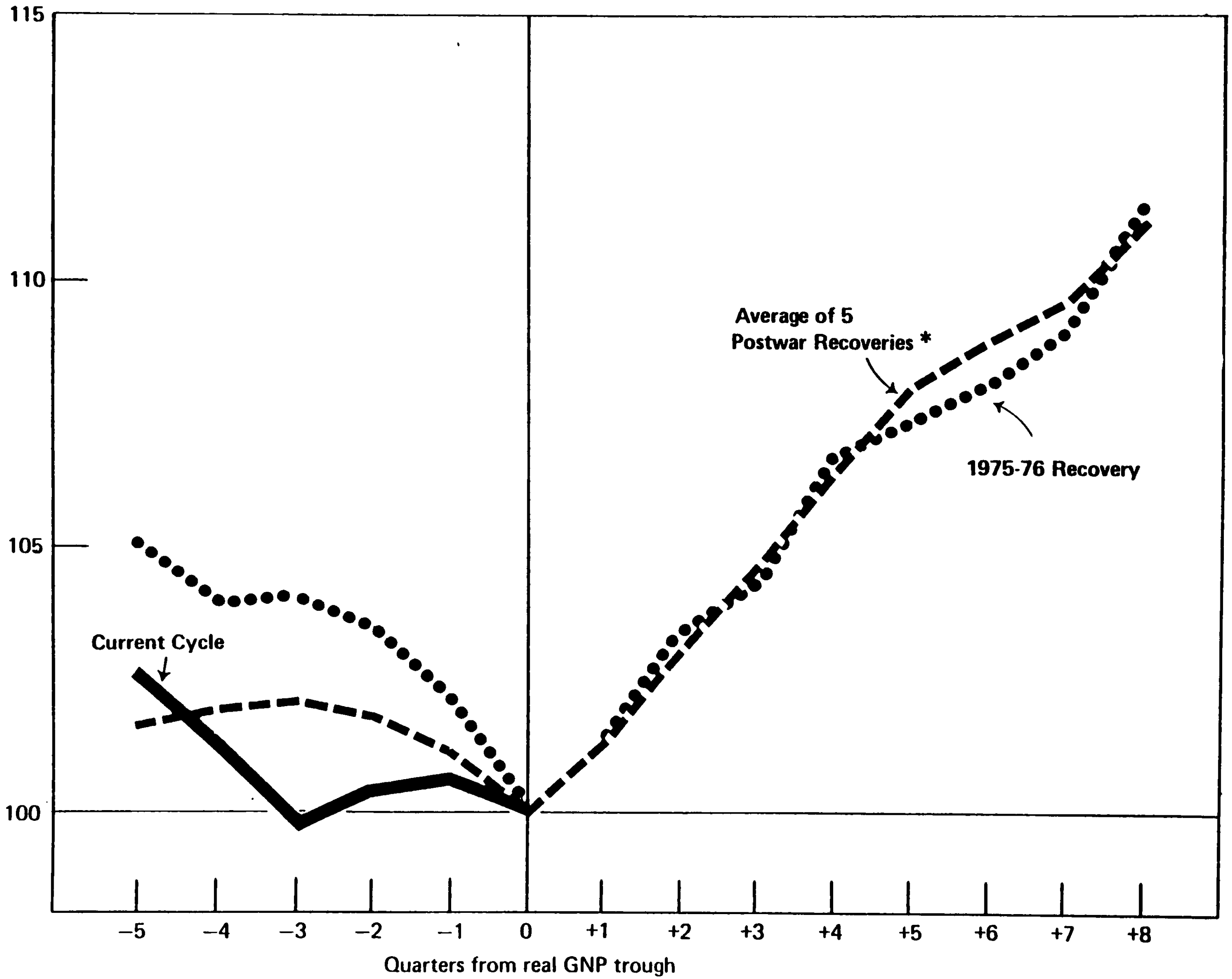


*Bank discount basis

February 14, 1983 A203

THE PATH OF POSTWAR ECONOMIC RECOVERIES

Real GNP trough = 100

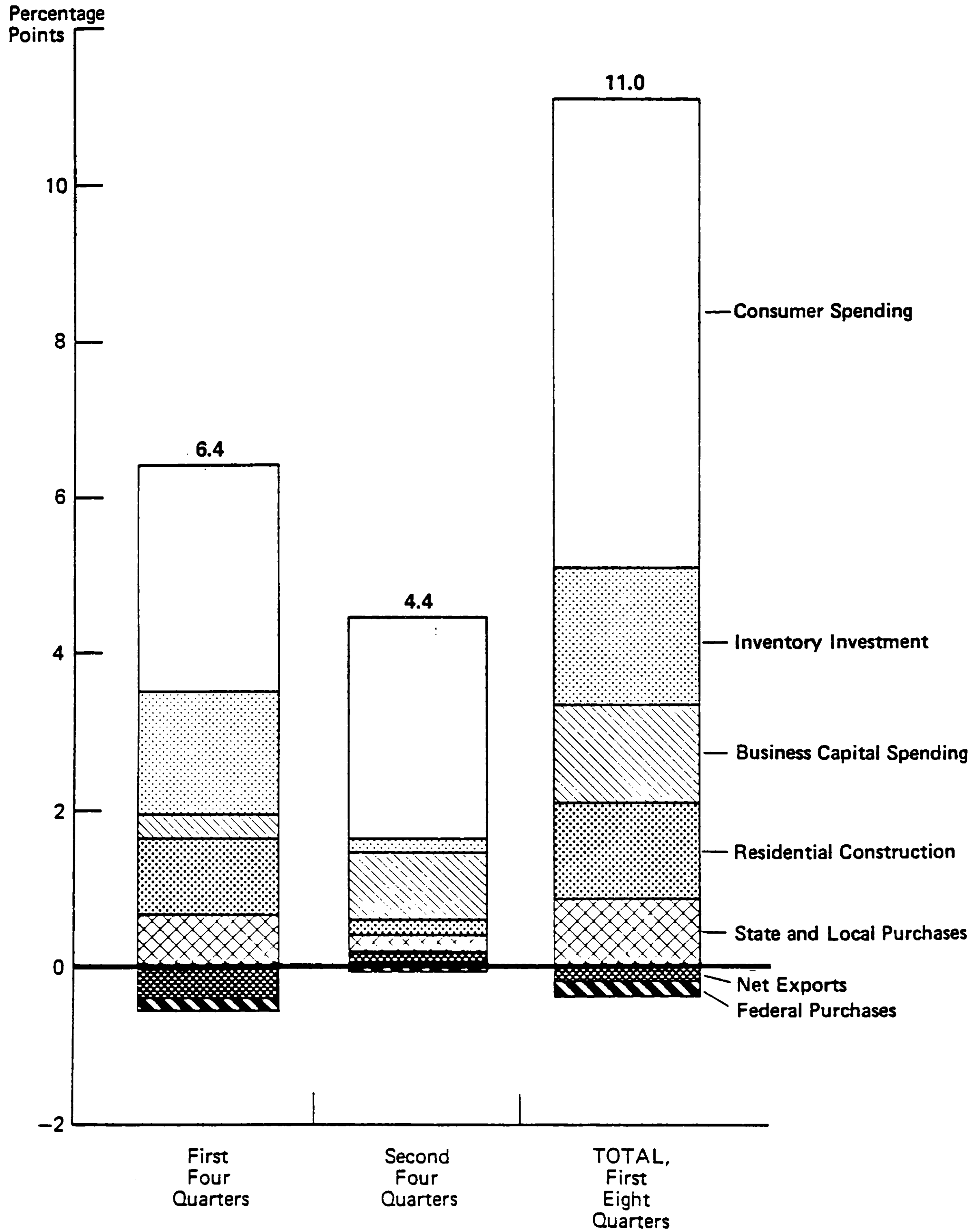


* Postwar recoveries excluding the Korean War period and the short-lived 1980-81 recovery.

January 25, 1983-A210

Chart IV

CONTRIBUTIONS TO A TYPICAL RECOVERY* BY REAL GNP COMPONENT

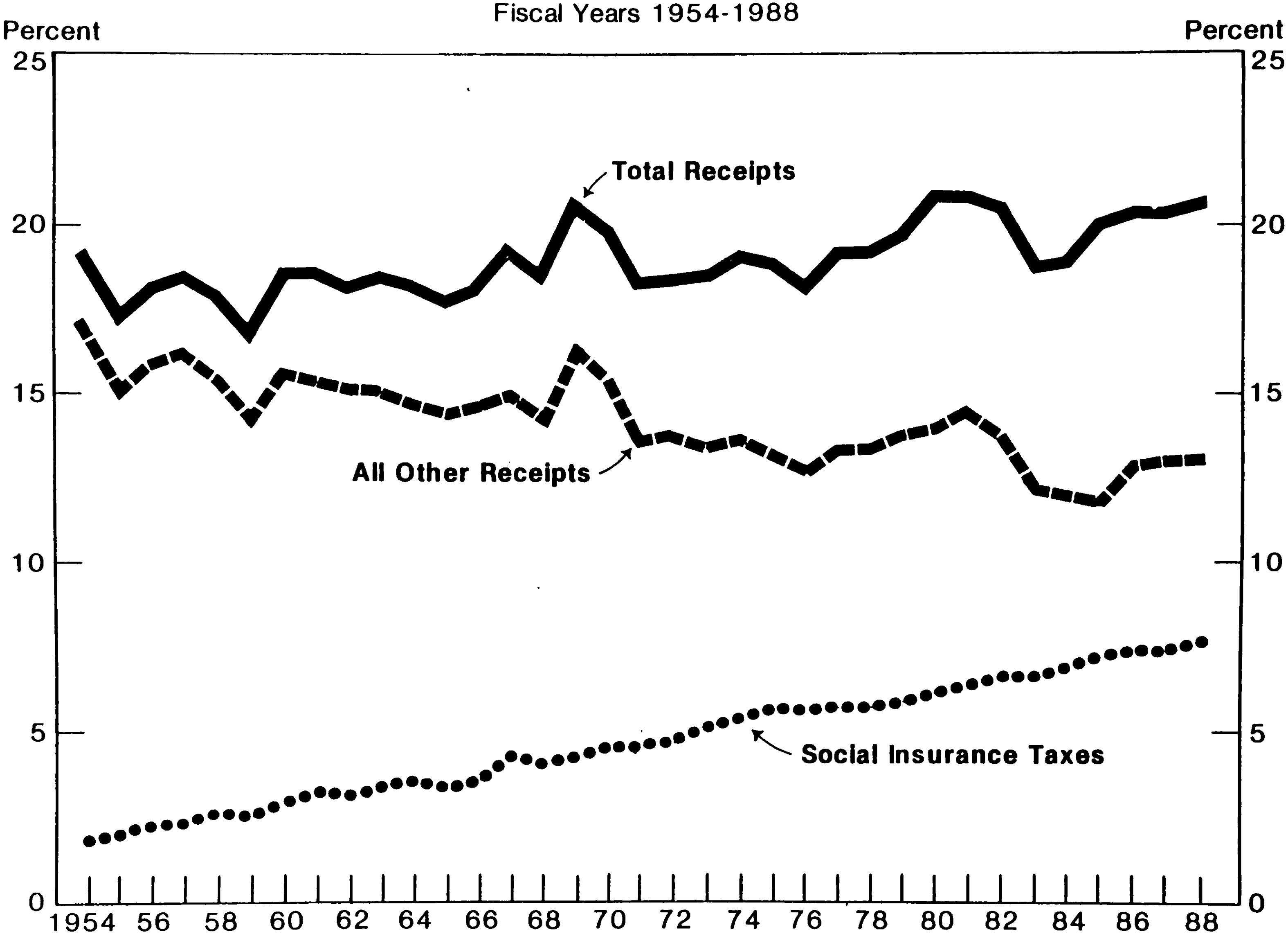


* Average of postwar recoveries, excluding the Korean War period and the short-lived 1980-81 recovery.

January 21, 1983-A213

UNIFIED BUDGET RECEIPTS AS A PERCENT OF GNP *

Fiscal Years 1954-1988

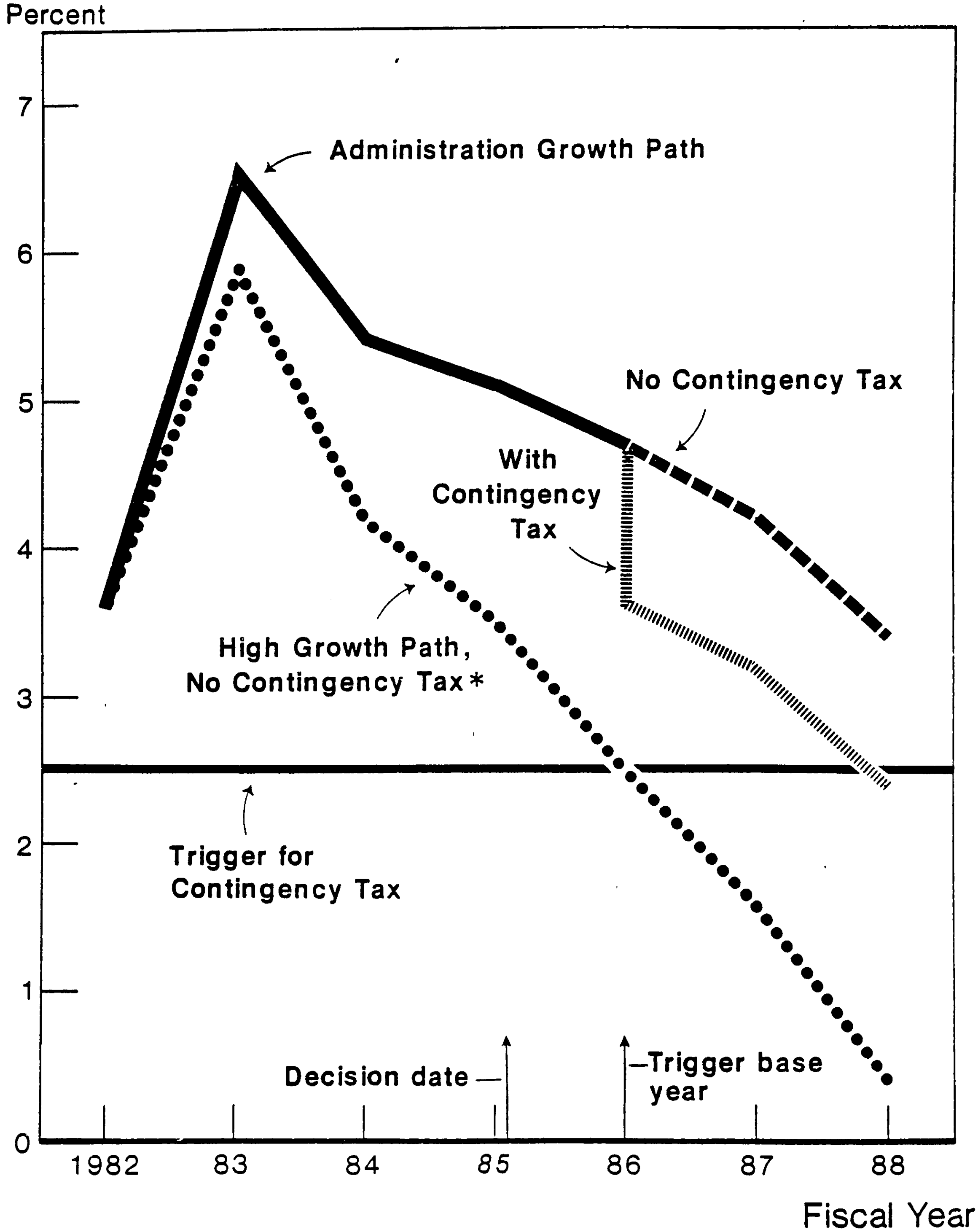


* Receipts include contingency taxes.

January 28, 1983-A215

Chart VI

THE DEFICIT AS A SHARE OF GNP



*Higher growth than the official path by 1-1/3 percentage point starting fiscal year 1983.

January 28, 1983-A214

TREASURY NEWS
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Statement by
Donald T. Regan
Secretary of the Treasury
February 11, 1983

The Interim Committee has reached agreement on the size and distribution of an increase in IMF quotas. The proposed increase in IMF quotas is 47.4 percent, from SDR 61.1 billion to SDR 90 billion.

As you know, agreement was also reached last month by the major industrial countries on a revision and expansion of the General Arrangements to Borrow (GAB).

For the United States, these agreements involve an increase in the U.S. quota in the IMF by about 5.3 billion, from SDR 12.6 billion to SDR 17.9 billion. At current exchange rates, this is equivalent to an increase of $5.8 billion, from roughly $13.8 billion to $19.6 billion.

Our portion of total new IMF quotas will be about 19.9 percent, compared to 20.7 percent at present. Our voting share will go from 19.52 percent to 19.17 percent.

The U.S. share of the expanded GAB will be SDR 4,250 million, 25 percent of the new total of SDR 17 billion. The U.S. commitment will, therefore, increase by the equivalent of about $2.6 billion, at current exchange rates.

We are very pleased with the agreement. It should provide sufficient resources to the IMF for it to carry out its responsibilities.

Two important factors bear on our view of this increase. First, in recent months the U.S. and others of the major industrialized nations have moved swiftly to provide short term assistance to the debtor nations. Secondly, we are seeing increasing signs of economic recovery, both in the U.S. and other parts of the world. This agreement today--when added to these two factors--will provide a strong foundation for increased confidence in world financial stability and future economic growth.

R-2033

It is important to view quota increases within the context of world economic conditions. In the 1970's, we witnessed periods of high and rising inflation and interest rates. Today, inflation is way down, interest rates are declining, oil prices are dropping. With this economic environment, we are even more confident than ever that these quota increases are sufficient for the foreseeable future.

Within a few days, we will be sending legislation to Congress requesting approval for the U.S. share of the IMF increase in resources. As Congress moves through its deliberations, I think it will become increasingly clear that this support for the IMF is in our own national interests.

The American economy operates in a world marketplace. Our recovery and the recovery of other nations are tied tightly together. The nations now in debt represent customers for our exports. Thus, they represent jobs here.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE

February 14, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $6,200 million of 13-week bills and for $ 6,203 million of 26-week bills, both to be issued on February 17, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing May 19, 1983			:	26-week bills maturing August 18, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	97.922	8.221%	8.51%	:	95.768 a/	8.371%	8.86%
Low	97.908	8.276%	8.57%	:	95.750	8.407%	8.90%
Average	97.913	8.256%	8.55%	:	95.759	8.389% 2/	8.88%

a/ Excepting 1 tender of $100,000.

Tenders at the low price for the 13-week bills were allotted 94%.
Tenders at the low price for the 26-week bills were allotted 17%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 39,315	$ 39,315	:	$ 79,315	$ 39,315
New York	12,427,230	4,955,610	:	12,372,350	5,286,860
Philadelphia	25,700	25,700	:	16,470	16,470
Cleveland	85,465	60,465	:	39,920	26,920
Richmond	45,610	40,310	:	104,315	61,505
Atlanta	51,825	51,825	:	37,310	36,810
Chicago	1,029,705	398,120	:	756,625	137,625
St. Louis	53,455	44,455	:	51,070	40,070
Minneapolis	14,310	14,290	:	12,825	10,825
Kansas City	38,580	38,580	:	51,620	48,175
Dallas	25,475	20,475	:	19,690	14,690
San Francisco	855,610	262,610	:	817,770	242,470
Treasury	248,250	248,250	:	241,030	241,030
TOTALS	$14,940,530	$6,200,005	:	$14,600,310	$6,202,765
Type					
Competitive	$12,902,705	$4,162,180	:	$12,258,315	$3,860,770
Noncompetitive	999,210	999,210	:	718,895	718,895
Subtotal, Public	$13,901,915	$5,161,390	:	$12,977,210	$4,579,665
Federal Reserve	967,515	967,515	:	950,000	950,000
Foreign Official Institutions	71,100	71,100	:	673,100	673,100
TOTALS	$14,940,530	$6,200,005	:	$14,600,310	$6,202,765

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 8.275%.

R-2034

TREASURY NEWS
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FOR RELEASE AT 4:00 P.M. February 15, 1983

TREASURY TO AUCTION $5,500 MILLION
OF 5-YEAR 2-MONTH NOTES

The Department of the Treasury will auction $5,500 million of 5-year 2-month notes to raise new cash. Additional amounts of the notes may be issued to Federal Reserve Banks as agents for foreign and international monetary authorities at the average price of accepted competitive tenders.

Details about the new security are given in the attached highlights of the offering and in the official offering circular.

Attachment

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R-2035

HIGHLIGHTS OF TREASURY
OFFERING TO THE PUBLIC
OF 5-YEAR 2-MONTH NOTES
TO BE ISSUED MARCH 1, 1983

February 15, 1983

Amount Offered:

To the public	$5,500 million

Description of Security:

Term and type of security	5-year 2-month notes
Series and CUSIP designation	Series H-1988 (CUSIP No. 912827 PF 3)
Maturity date	May 15, 1988
Call date	No provision
Interest rate	To be determined based on the average of accepted bids
Investment yield	To be determined at auction
Premium or discount	To be determined after auction
Interest payment dates	November 15 and May 15 (first payment on November 15, 1983)
Minimum denomination available	$1,000

Terms of Sale:

Method of sale	Yield Auction
Competitive tenders	Must be expressed as an annual yield, with two decimals, e.g., 7.10%
Noncompetitive tenders	Accepted in full at the average price up to $1,000,000
Accrued interest payable by investor	None
Payment by non-institutional investors	Full payment to be submitted with tender
Deposit guarantee by designated institutions	Acceptable

Key Dates:

Deadline for receipt of tenders	Wednesday, February 23, 1983, by 1:30 p.m., EST
Settlement date (final payment due from institutions)	
a) cash or Federal funds	Tuesday, March 1, 1983
b) readily collectible check	Friday, February 25, 1983

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-204

FOR IMMEDIATE RELEASE
February 16, 1983

Contact: Marlin Fitzwater
(202) 566-5252

STATEMENT BY
DONALD T. REGAN
SECRETARY OF THE TREASURY
ON INDUSTRIAL PRODUCTION
WEDNESDAY, FEBRUARY 16, 1983

The January rise in industrial production is another important signal that recovery is in progress.

Led by increased output of autos and homegoods, industrial production rose a revised 0.1 percent in December, and a strong 0.9 percent in January.

Historically, the upturn in industrial production has marked the end of recessions. While it is too early to predict whether this is the case with the present recession, the positive swing in industrial production along with encouraging developments in housing, retail sales and inventories reinforces the foundation for a strong consumer-led recovery.

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TREASURY NEWS

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TREASURY DEPARTMENT

Remarks by
The Honorable
Deputy Secretary R. T. McNamar
Chicago Savings Bonds Volunteer Committee
Hyatt Regency Hotel, Chicago, Illinois
Tuesday, February 15, 1983

Thank you, Bob, for that kind introduction. I am happy to be here today to break bread with friends from the business community. I'm also happy to be with all of you to open the Chicago Area's 1983 Savings Bonds Payroll Savings Campaign.

First, I would like to point out the key features of our new Savings Bonds program and why it should fit into the average American's plans for savings and investment.

Second, I would like to discuss briefly the Reagan Administration's economic policy including signs that the economy is turning around.

And finally, I would be delighted to use the remaining time to field your questions.

Nineteen Eighty Three is a very upbeat year for Savings Bonds. The new variable, market-based rate is the most significant and most exciting change in Savings Bonds in more than 40 years. It represents a dramatic new incentive to save, and ensures a positive competitive rate of return in what has been a stormy savings environment.

One of your colleagues -- Jim Robinson, Chairman and Chief Executive Officer of American Express and the Chairman of the 1983 U. S. Savings Bonds Volunteer Committee -- calls Savings Bonds "one of the best investments in the country."

Jim supported this view with his own full page ad in the Wall Street Journal on February 4. By the way, the ad lists Bob Reuss of Centel Corporation and the other members of the 1983 Savings Bonds Volunteer Committee.

Since 1935, Savings Bonds have been an important stabilizing force in our Nation's debt-management efforts. Sales of Bonds help the Treasury reduce the interest costs of the debt to all taxpayers. Bond sales also help reduce the Treasury's need to borrow in the open market, thereby reducing pressures on all interest rates from Federal borrowing.

When Americans cut back on the Savings Bonds habit, there is more pressure on the Treasury to borrow elsewhere. Increased Treasury borrowing, in turn, drains funds that otherwise would be available for private investment. More participation in the Savings Bonds Program will help remove that pressure. It spreads the debt to people who are not otherwise involved in the credit markets. As Jim says in his ad, "Research shows that the payroll saver buys U. S. Savings Bonds when he wouldn't otherwise save."

Savings Bonds are cost effective for our Government because they pay less interest than Treasury marketable securities and because they are held more than twice as long as the marketable portion of the national debt. This means that the Savings Bonds portion of the debt does not have to be refunded as often as the remainder of the debt -- for example, our 13, 26, and 52-week bills and our two and three year notes. All Americans, therefore, benefit from this reduction in interest expense and from the relative stability that Savings Bonds offer.

Today, Americans hold more than $68 billion worth of Savings Bonds. That is $68 billion the Government does not have to borrow in the open market. That permits new savings the private sector can pour into new ideas, new products, and new jobs that will lead the Nation into a future that is bright and prosperous.

Some 80 percent of all Savings Bonds sales are through the payroll savings plan. The plan has prospered through the support of thousands of business leaders like you who promote and operate payroll savings plans. The result has been the enthusiastic participation of employees who find it the one sure way to accumulate reserves for their future.

Payroll savings provide a widespread, easy, convenient, and systematic way to safely put money away. Through this plan, money is saved at the source -- the paycheck -- before the money is in hand and one is tempted to spend it.

This may not be the most sophisticated way to save, but it is pragmatic, and it works. With $4 of every $5 in Savings Bonds coming through payroll savings, the plan has spearheaded the Bond program's tremendous contribution to the American economy.

The payroll savings program historically has been an ideal model of government-private sector cooperation. In fact, in the minds of many Americans, Savings Bonds and payroll savings are one and the same. Millions of people have never purchased a Bond in any other way. Certainly the widespread ownership of government securities could not have been accomplished without this automatic thrift plan.

Offering payroll savings in your companies -- and volunteering to convince other business leaders to do the same -- is the key to a successful Bond program.

How else can an individual earn market-based rates -- currently over 11 percent on Savings Bonds -- for as little as $25, with minimal effort? For that amount of money, the saver also gets a guaranteed minimum return -- 7½ percent. He is free from state and local income taxes. He can defer reporting the interest on his Federal return until the Bonds are cashed. And his principal and interest are guaranteed safe.

Think about it:

11% rate-4% CPI = 7% real return.

7½% minimum-4% CPI = 3.5% real return.

No state and local taxes.

Tax deferred on Federal.

But no matter how good the product -- no matter how attractive the interest rates -- the success of the program still rests with you: the individual.

I'm here today on behalf of President Reagan and Secretary Regan to thank you personally for spearheading vigorous payroll savings campaigns in your companies. Your executive leadership skills will help sell your employees on the merits of Savings Bonds and on the convenience of payroll savings. No one else can do it. Without your strong and enthusiastic efforts, Bond sales will not keep pace with our Nation's financing needs.

We need a strong Savings Bonds Program. The health of our Nation depends on it. And the success of the Bond Program -- in turn -- relies heavily on payroll savings.

A strong payroll savings campaign will sign up people who have never bought Bonds before. It will sign up those who have no savings plans at all -- and sign up the more sophisticated savers who have ignored Savings Bonds in the past because they felt they could get more for their money elsewhere. Such a campaign will also encourage present payroll savers to increase their payroll deductions for Bonds. When 1984 rolls around, I predict that you will be looking back and say:

> "This was a great year for the Savings Bonds Program, and my personal efforts helped to lower interest rates for all Americans."

Now, I would like to direct my remarks to the progress of our economy and the encouraging signs we see for economic recovery. As we enter this new stage, your businesses will play a significant role. It is you who will be making the critical decisions on where and when and how much to put into capital investment, when to rehire and alike. These decisions will be far-reaching because they determine down the road the productivity and competitiveness of your products in the marketplace and this in turn reflects on your level of employment, earnings, and overall success of your business.

The development of a sound fiscal and monetary policy was the central objective of the Reagan Administration when it came to office two years ago. Year after year, Americans watched as an increasing share of the Gross National Product was allocated for Federal spending and taxes. As the Government siphoned off more and more capital from the private sector and the money supply expanded, economic activity stagnated and inflation soared.

Early in this Administration, President Reagan put before Congress a four point plan to revitalize the American economy, and with it the worlds' economies. His program mandated that:

- First, we must stop irresponsible and inflationary spending. Federal programs must be pruned to fit financial reality. In short, we've got to cut unnecessary government spending.

- Second, we must reduce excessive taxation because it suffocates individual incentive and productivity in the private sector. Raising taxes on working

Americans does not solve our Government spending problems. One of the lessons I have learned in Washington is that Big Government does not tax to get what it needs -- it taxes to get what it wants. Somehow, someway, our Government has an uncanny ability of spending all the money it can get its hands on -- and then some.

. Third, we must replace the irregular monetary habits of the past with consistent non-inflationary practices. One of the great concerns of business leaders in the country has been and continues to be the fear of volatile movements in money growth -- on the one hand, swelling the money supply too fast, spinning us back into the inflationary cycle, and on the other hand, shrinking it too rapidly, giving us a protracted recession. Our aim is to achieve a monetary policy that is accommodative enough to provide consistent, sustainable, but non-inflationary economic growth.

. Fourth, we must make major reductions and improvements in government regulations. Regulation upon regulation written in Washington -- measuring tens of thousands of pages in the Federal Register -- has reduced the flexibility and productivity of our society and has crippled its ability to respond rapidly to changes in the marketplace. We have made a good start in this regard, but much more needs to be done. We want to return more decision making to State Street and get it off Pennsylvania Avenue.

President Reagan inaugurated his program with the comment:

> "It's not my intention to do away with Government. It is rather to make it work -- work with us, not over us; to stand by our side, not ride our back."

Where are we?

In the past 24 months, we have implemented major portions of the President's plan. The task now is to encourage the renewal of economic growth to reduce unemployment and provide productive job opportunities in the private sector. But we must do this thoughtfully and not repeat the errors of the past and return to an inflationary economy.

On the brighter side, we do have clear signals that our U.S. economy is turning around and that the recession will soon be behind us. Unfortunately, the upturn has been much longer in coming than we -- or most forecasters -- had expected. The delay in recovery occurred primarily because of the persistence of high interest rates and the weakening economies of our leading trading partners.

When times were good, our exports accounted for one out of three acres of U.S. agricultural production, one out of eight manufacturing jobs, and nearly 20 percent of U.S. production of all goods. Because of poor economic growth, high unemployment, and the alarming debt scheduling problems of many countries, our trade deficit has widened from $28 billion in 1981 to $36 billion in 1982, and a projected $65-75 billion in 1983.

The weakness in exports -- combined with a general hesitancy on the part of the U.S. consumer -- has led to slow buying, a drop in consumption, and a delay in the expected turnaround of the economy.

Now, here are the encouraging signs we see that the recovery is underway and that the recession will soon be behind us:

- The index of leading indicators has risen for eight out of the last nine months.

- Housing is in the midst of a rapid recovery.

- Business trimmed inventories sharply in the final quarter of last year. Historically, a cleanout of inventories typically has been followed by a shift back to higher rates of production.

- Durable goods spending is up.

- Retail sales have begun to climb.

- Total industrial production stabilized in December and appears poised to turn upward.

- The index of average hourly earnings of production workers in the private nonfarm economy rose at a 5.1 percent annual rate last month from 6 months earlier and was up 5.4 percent from 12 months earlier.

- The unemployment rate fell to 10.4 percent (representing 11.4 million workers) last month from 10.8 percent (12 million) in December.

- Claims for new unemployment have fallen steadily.

- Commodity prices have shown some firming in recent weeks.

As economic recovery gets underway, there are certain conditions that we must not revert to. We must not revert to the overly stimulative monetary and fiscal policies pursued at times in the past -- for these would surely lead to a resurgence of inflationary pressures and a new round of rising interest rates.

Further -- despite some political demands to the contrary -- we must not reverse the fundamental tax restructuring put in place in 1981, for these tax improvements are designed to provide the non-inflationary incentives to fuel the economic engines of the private sector. In this regard, we welcome Chairman Rostenkowski's comments that the third year of the tax cut scheduled for July 1, 1983, should go into effect. We hope he will see the wisdom of not tampering with indexing of taxes as well.

In closing, I want to assure you that the Administration's program of steady money supply, new tax philosophy, fewer regulations, and budget cuts is now clearly working.

It is working, but working slowly. Success won't occur overnight. We are dealing with the most complicated economy in the world, but fortunately the best.

The real danger is that the cycle of economic change and the cycle of American patience too often are at odds. It takes time to turn economic trends around while public opinion too often wants instant results to longstanding problems.

Disinflation and sustained economic growth don't make good footage for the seven o'clock news. Unemployment and impatience do. Human hardships and change are emotional, and require compassion from all of us.

Those of you with teenage sons and daughters should listen to the lyrics of the popular singer Billy Joel when he sings the new top hit record, "Allentown". It says a lot about how people feel today about jobs, going to college, the American work-ethic and economic change.

Yet, change we must if we are to have a renewal of sustained prosperity and abandon the stop and go economic policies of the past quarter century. We must change our anticipations about energy prices, about inflation, about pay increases, about savings, and about the Government's ability to do all things overnight without an adverse impact on the economy.

The American economy is like a large oil tanker in mid-ocean. It has enormous momentum to continue going the same direction. But the captain of the ship of state -- the President -- has ordered the change and the bow has begun to swing around and point to a new period of sustained noninflationary prosperity. We have set a new course. And we will stay that course.

To close by returning to where I started, the new variable rate savings bond plays an important part in ensuring that we can finance our Government in the most efficient way with the least pressure on short-term interest rates. So you who are the business, Government, and labor leaders of Chicago, have a key role to play in helping to keep interest rates declining and to thereby promote the recovery. We've changed our product, now we need you to change people's attitudes by showing them the benefits of the new savings bond.

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TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE February 16, 1983

RESULTS OF AUCTION OF 2-YEAR NOTES

The Department of the Treasury has accepted $7,501 million of $14,934 million of tenders received from the public for the 2-year notes, Series R-1985, auctioned today. The notes will be issued February 28, 1983, and mature February 28, 1985.

The interest rate on the notes will be 9-5/8%. The range of accepted competitive bids, and the corresponding prices at the 9-5/8% interest rate are as follows:

	Bids	Prices
Lowest yield	9.65%	99.955
Highest yield	9.73%	99.813
Average yield	9.71%	99.849

Tenders at the high yield were allotted 94%.

TENDERS RECEIVED AND ACCEPTED (In Thousands)

Location	Received	Accepted
Boston	$ 83,660	$ 49,760
New York	12,443,940	6,127,270
Philadelphia	46,080	46,080
Cleveland	179,995	164,635
Richmond	138,490	117,420
Atlanta	71,650	61,590
Chicago	768,075	360,235
St. Louis	129,775	122,185
Minneapolis	63,430	62,130
Kansas City	97,955	95,895
Dallas	35,510	35,330
San Francisco	872,130	255,110
Treasury	3,110	3,110
Totals	$14,933,800	$7,500,750

The $7,501 million of accepted tenders includes $1,455 million of noncompetitive tenders and $6,046 million of competitive tenders from the public.

In addition to the $7,501 million of tenders accepted in the auction process, $340 million of tenders was awarded at the average price to Federal Reserve Banks as agents for foreign and international monetary authorities. An additional $499 million of tenders was also accepted at the average price from Government accounts and Federal Reserve Banks for their own account in exchange for maturing securities.

R-2038

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE February 17, 1983

RESULTS OF TREASURY'S 52-WEEK BILL AUCTION

Tenders for $ 7,750 million of 52-week bills to be issued February 24, 1983, and to mature February 23, 1984, were accepted today. The details are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:

	Price	Discount Rate	Investment Rate (Equivalent Coupon-issue Yield)
High -	91.626	8.282%	8.96%
Low -	91.588	8.320%	9.01%
Average -	91.600	8.308%	8.99%

Tenders at the low price were allotted 55%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted
Boston	$ 85,370	$ 41,370
New York	15,290,600	6,918,350
Philadelphia	8,720	6,720
Cleveland	121,280	72,120
Richmond	64,435	24,125
Atlanta	153,890	47,390
Chicago	771,905	131,715
St. Louis	94,535	45,535
Minneapolis	11,900	10,900
Kansas City	21,010	20,510
Dallas	11,000	6,000
San Francisco	1,573,610	358,360
Treasury	67,160	67,160
TOTALS	$18,275,415	$7,750,255
Type		
Competitive	$16,324,925	$5,799,765
Noncompetitive	555,490	555,490
Subtotal, Public	$16,880,415	$6,355,255
Federal Reserve	1,200,000	1,200,000
Foreign Official Institutions	195,000	195,000
TOTALS	$18,275,415	$7,750,255

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TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
February 18, 1983

Contact: Charles Powers
(202) 566-2041

TREASURY ANNOUNCES PUBLIC MEETING TO DISCUSS
U.S.-FINLAND TAX TREATY ISSUES ON MARCH 7, 1983

The Treasury Department today announced that it will hold a public meeting on March 7, 1983, to solicit the views of interested persons regarding issues to be considered during negotiations of new income tax and estate tax treaties between the United States and Finland.

The public meeting will be held at the Treasury Department, at 2:00 p.m., in room 4125. Persons interested in attending are requested to give notice in writing by March 1, 1983, of their intention to attend. Notices should be addressed to Leslie J. Schreyer, Deputy International Tax Counsel, Department of the Treasury, Room 4013, Washington, D.C. 20220.

Today's announcement of the March public meeting precedes a second round of negotiations between representatives of the United States and Finland to develop a new income tax treaty for the avoidance of double taxation and the prevention of tax evasion and precedes the first round of negotiations between such representatives to develop a new estate tax treaty. The existing income tax treaty between the United States and Finland was signed in 1970, and the existing estate tax treaty between the two countries was signed in 1952.

The Treasury seeks the views of interested persons in regard to the full range of income tax and estate tax treaty issues, as well as other matters that may have relevance to the tax treaties between the United States and Finland. The March 7 public meeting will provide an opportunity for an exchange of views and will permit discussion of the United States position in regard to the issues presented.

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R-2040

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-204

STATEMENT OF BERYL W. SPRINKEL
UNDER SECRETARY OF THE TREASURY FOR MONETARY AFFAIRS
BEFORE THE
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE
WASHINGTON, D. C.

Tuesday, February 22, 1983

Chairman Garn, Senator Proxmire, distinguished Members of the Committee, it is my pleasure to be here today to present Treasury's views on current monetary policy, and to discuss your concerns and questions on the subject.

Monetary Policy in 1983

The task for monetary policy in 1983 appears to be clear. Chairman Volcker stated it well in his testimony before this Committee last week when he said, "Our objective is easy to state in principle -- to maintain progress toward price stability while providing the money and liquidity necessary to support economic growth." From my discussions with other Administration officials, Federal Reserve officials, businessmen and economists, and from my reading of the financial press, there appears to be widespread, general consensus that this is the appropriate goal for monetary policy in 1983 and the targets set by the Federal Reserve are broadly consistent with that goal. But general agreement does not, in and of itself, produce the desired results. If it did, we presumably would not have had a decade and a half of rising inflation and interest rates and the resultant economic stagnation; certainly no one sought or desired those results.

The subtleties and complexities of monetary control are such that achieving a particular desired policy path -- regardless of a consensus that it is appropriate -- is never a certainty. Our knowledge of the exact magnitude and timing of the impact of monetary actions is imperfect; the lag in their impact on the economy is variable. For either -- or a combination of both -- of these reasons, there is always a risk that actual monetary policy will not match intentions or goals.

Without great care in the implementation of monetary policy in the coming months, there is a risk that the Federal Reserve could err in one direction and be too highly restrictive, or in the other direction, and be overly expansionary. The danger to the economy is that the economic recovery could be aborted, or the gains we have made in reducing inflation could be lost, or both. It is these risks and dangers that I would like to discuss with you today.

R-2041

First, I believe it would be instructive briefly to review where we are, and how we arrived where we are, with respect to monetary policy.

The General Situation

A deceleration in the trend rate of money growth is necessary to reduce inflation; it is for this reason that the Administration originally recommended that money growth be gradually and steadily slowed. When I met with this Committee last July, I emphasized the importance of the gradual and steady aspect of that recommendation. Few believed that the slowing of money growth necessary to control inflation could be achieved without some associated restraint on the growth of economic activity; but we did believe that a gradual and steady deceleration would minimize the constraint on the economy, and that that constraint might be offset in the long run by the incentive effects of the tax cut. However it is difficult to characterize the slowdown in money growth that actually occurred as either gradual or steady. As a consequence, while impressive progress has been made on inflation, the restriction of economic activity associated with that progress was magnified.

In 1981, money growth was abruptly and significantly reduced relative to its previous growth path; after four years of money growth that averaged 7.8%, M1 growth in 1981 was 5%. For calendar 1981, M1 growth was therefore below the target growth range set by the Federal Reserve. After a short period of rapid growth in late 1981 and early January 1982, the restraint on money growth continued until mid-summer of 1982. By mid-1982, the path of M1 was well below the deceleration path that had been recommended by the Administration. This severe and prolonged monetary restriction was an important factor contributing to the onset, severity and duration of the recession.

By contrast, since July of 1982 money has grown at a very rapid pace; during the last quarter of the year, M1 grew at an annual compound rate of nearly 14%. As a consequence, M1 growth in 1982 averaged 8-1/2%, well above the 5-1/2% path that was the upper bound of the Federal Reserve's money growth target.

On the positive side, the monetary surge in the last half of 1982 can be viewed as an abrupt and belated adjustment for the previous, prolonged undershooting. The rapid pace of money growth in recent months, in fact, brought the fourth-quarter, 1982 average of M1 up to the level that was implied by the Administration's originally recommended path for prudent noninflationary monetary policy. Although we arrived at approximately the same average level for M1 by the fourth quarter of 1982, the path by which we did so was less than ideal.

An important lesson to be learned from the experience of recent years is that we pay a very high and very real price for monetary instability. The timing of the relationship between money growth and real economic activity is affected by a variety of factors, including the public's expectations about fiscal and monetary policies. Because of the elusiveness of expectations, any exact quantification of the economic impact of erratic money growth could be disputed; however, the direction of the effect seems clear. In short, while monetary policy seems to many to be academic and arcane, the effects of monetary actions are neither. The impact of monetary actions is felt in very practical and real ways -- as manifested in inflation, interest rates, real economic growth and the unemployment statistics.

Looking to the future, the monetary actions taken by the Federal Reserve will, as they have in the past, be critically important to economic performance in 1983-84. Obviously we can all agree that nurturing an economic recovery is our primary concern. But it is also vitally important that that recovery be a healthy and sustainable one, rather than either a recovery that stalls out quickly, or one that consists of an inflationary burst of economic activity that falters as inflationary expectations drive interest rates up and choke off expansion.

The challenge is to pursue policies that will provide the atmosphere needed for a sustainable, noninflationary economic expansion. With the rapid rate of money growth that has occurred in the last six months, the risks associated with monetary policy are that either (1) the monetary expansion would be abruptly curtailed, restraining output and employment growth as it did in 1981-82; or (2) the Federal Reserve would allow the monetary expansion to continue too long, reigniting inflationary expectations, driving long-term interest rates up and preventing a sustained recovery. Great care in the implementation of monetary actions will be needed if both these pitfalls are to be avoided.

The Danger of Being Overly Restrictive

It would be ill-advised for the Federal Reserve to attempt to reverse the bulge in money that has occurred in the last few months. Such a monetary contraction would almost certainly stall any meaningful economic recovery, and could, depending on its severity and duration, plunge the economy into a deeper recession.

However, it is clear that money growth cannot continue at the pace of the last quarter without precipitating economic disaster. The risk, however, is that an attempt to slow money growth may result in too severe, or too prolonged, a monetary squeeze. In the past, periods of rapid money growth have typically been followed by long periods of restriction. A prolonged period of slow money growth would again curtail the growth of employment and output as it did in 1981-82.

The challenge of reinstating noninflationary monetary policy is to bring down the long-run trend of money growth gradually enough that the restriction of economic activity is avoided.

permanent and continued progress toward lower inflation and interest rates requires that we persevere in our efforts to bring the trend of money growth back to a noninflationary pace. But, after six months of very rapid money growth, great care must be taken that those efforts do not result in another severe and lengthy restraint of money growth. Economic expansion cannot proceed without the support of adequate liquidity.

The Danger of Excessively Stimulative Monetary Policy

An economic recovery based on highly stimulative monetary policy is ultimately unsustainable, because the inevitable consequence of excessive money growth is inflation and rising interest rates, both of which are powerful deterrents to the long-run real economic growth we all seek. Rapid money growth does provide a stimulus to nominal GNP growth; a crucial concern, however, is whether that nominal income growth consists of real economic expansion (growth of real GNP), or of inflation. Rapid money growth may provide a temporary, short-lived stimulus to the economy, but once inflation and inflationary expectations emerge, real growth is choked off by rising interest rates. Once that point is reached, continued stimulative monetary policy is predominantly inflationary.

The key is the reaction of interest rates to the increase in money growth. If the financial markets fail to recognize the implications of rapid money growth, the rise in interest rates might be postponed, and the positive, stimulative effect of monetary expansion could last longer. But the more quickly inflationary expectations, and therefore interest rates, react, the more ineffective monetary expansion will be in providing economic stimulus. As has been illustrated often in recent years, interest rates and money growth can and do move in the same direction when market expectations and uncertainty about inflation are sensitive to the inflationary implications of increases in the money supply.

In this sense, recent developments in the financial markets contain some foreboding signals. Chart 1, accompanying my prepared testimony, illustrates the recent course of a representative short-term and long-term interest rate. While it is widely believed that the decline in interest rates that occurred last summer was the result of a more accommodative Federal Reserve policy, this is not really an accurate portrayal of the timing of events. Money growth began to accelerate in August and, as can be seen in the chart, most of the decline in interest rates had already occurred by August. Some short-term rates are now slightly lower than they were in late August, but the three-month Treasury bill rate is slightly higher now than it was the last week in August. The decline in long-term rates continued into the fall, but then levelled off; long rates have risen slightly in the last few months.

Therefore while the rapid growth of bank reserves provided by the Federal Reserve in recent months did push short-term interest rates down to some extent, attempts to continue to do so are likely to be self-defeating. We have already seen a leveling off of short-term rates despite continued rapid reserve and money growth; the last decrease in the discount rate did not elicit similar decreases in short-term market rates. As Chairman Volcker has stated on many occasions, the Federal Reserve has no button to push to cause interest rates to fall.

In terms of its long-run implications, the failure of long-term rates to follow short rates down and the recent upturn in long rates, despite continued rapid growth in reserves and money, is a foreboding signal of the financial markets' expectations. The only logical explanation of this development is that the financial markets are observing current reserve and money growth and making some calculation about expected, future inflation -- or at least some calculation of their fear or skepticism about future inflation. Inflationary expectations is the only plausible connection between short-run changes in money growth and long-term interest rates. Thus, while it may be possible for the Federal Reserve to temporarily push down, or hold down, short-term interest rates by injecting more reserves into the banking system, such actions are not likely to generate the desired decreases in long-term rates; under certain market conditions, even the desired declines in short-term rates may not materialize.

A key element in the behavior of long-term rates is inflationary expectations. In the current situation, the uncertainty about the budget situation and about long-run inflation control has heightened the sensitivity of inflationary expectations. The uptick in long-term rates in recent months may be the first signal that, from the viewpoint of the financial markets, the monetary expansion has gone too far.

This is the danger of using excessively expansionary money growth in an attempt to stimulate the economy. There may be limited short-term success, as long as long-run inflationary expectations do not move adversely. But predicting the timing of those expectations with any degree of precision is impossible; helpful, stimulative money growth ultimately turns into excessive money growth that drives inflationary expectations and interest rates upward and precludes continued, real economic expansion.

The path of long-term interest rates will be a critical factor in determining whether or not the incipient recovery will evolve into a period of sustained real economic growth. In my view, one of the most troublesome developments over the past decade and a half has been the successive upward drift of long-term interest rates. Chart 2 illustrates the upward trend of long rates over the past twenty-five years and relates it to the rising trend rate of money growth. While there have been many periods when long-term rates fell -- notably during or directly after recessions -- the low point of each downturn in long-term rates has been higher than the previous one. Each upturn has taken long rates to new highs, and each successive low point has been at a level higher than the preceding low point. The rising trend of inflation and long-term interest rates has most likely contributed to our long-run problems of lagging investment and productivity growth.

The most important message in Chart 2 for the current situation is that we have not yet broken this pattern. While long-term rates are now well below their all-time highs reached in 1981, they have not yet broken below their previous cyclical low, which, from a historical standpoint, was not particularly low. Despite the significant decline in inflation, we have not yet succeeded in breaking the trend of secularly rising long-term interest rates. The implications of this for long-run, real economic growth are not encouraging.

The behavior of long-term rates and their reaction to money growth is the immediate and practical danger of continuing rapid money growth. Attempts by the Federal Reserve to push down, or hold down, short-term interest rates would require continued rapid growth of reserves and money. Particularly as the economy grows more strongly and credit demand increases, upward pressures on short-term rates will emerge; more and more reserve growth would be required to hold down short-term interest rates in the face of these market pressures. Ultimately, the resulting money growth would aggravate inflationary expectations and cause long-term rates to rise, thereby defeating the intended goal of encouraging lower interest rates.

Where Do We Go From Here?

With economic dangers lurking both on the side of too much money growth, and on the side of too much restraint, the safest course is to provide moderate money growth. That is, of course, easier to state than it is to achieve. The chances of achieving that goal, however, would be maximized if the Federal Reserve would move now to restrain the growth of bank reserves in order to slow money growth gradually from the high rates of recent months. Efforts by the Federal Reserve to peg or reduce short-term interest rates are not likely to produce that result.

Actions to return reserve growth to a rate consistent with moderate money growth may cause immediate, but temporary, increases in short-term interest rates. Bank reserves have grown very rapidly for many months, so upward pressure on short-term rates is the price we now may have to pay to restore more moderate growth and to protect long-term rates from the large increases that are inevitable if reserve and money growth is not moderated.

There are many who contend that more rapid money growth now is acceptable because of the weakness of the economy and because it can be reversed later on, once the recovery is more strongly underway. This view presumes that sometime in the future will be the "right time" for bank reserve and money growth to be easily, conveniently and painlessly brought back under control. Furthermore, this analysis makes some heroic assumptions about the precision of monetary control and economic forecasting.

Continuing to allow rapid money growth in order to stimulate economic recovery presumes that the monetary authority can apply the appropriate dose of monetary stimulus for just long enough to provide expansion, but neither too much, nor for too long, to generate more inflation and inflationary expectations. Given the inaccuracies of economic forecasting and the deficiencies in our knowledge about the timing and impact of monetary actions, it is extremely difficult to determine the moment when helpful stimulus becomes harmful and inflationary. Furthermore, even if that moment could be accurately determined, such fine-tuning policies presume a precision for monetary control that could, but unfortunately, does not exist. Such monetary fine-tuning sounds logical and reasonable in casual conversation, but it is extremely difficult to achieve; it has not worked reliably in the past and the attempts on average have been very destabilizing.

The money growth target ranges for 1983, announced by Chairman Volcker last week, are consistent with our goal of providing enough money growth to support the expansion, without reigniting inflationary pressures. While the ranges set for M1 and M2 for 1983 are higher than their 1982 ranges, these adjustments were made in order to account for the effects of institutional change. Changes in the money supply that are the result of institutional change have no particular economic meaning. It is therefore appropriate to adjust the money growth targets to take account of these changes, as they can best be estimated at this time. The Federal Reserve has stated that the new targets, after adjustment for institutional change, are comparable to the 1982 targets in terms of economic meaning.

With respect to the new targets, Chairman Volcker said in his statement that "... the growth of money and credit will need to be reduced to encourage a return to reasonable price stability. The targets set out are consistent with that intent." The Administration agrees with that goal and intent. Since money growth exceeded the targets in 1982, average money growth will be lower in 1983 if the new target ranges are achieved; this is consistent with the goal, shared by the Administration and the Federal Reserve, of noninflationary money growth over the long run.

Conclusion

The sustained, noninflationary economic expansion that we all desire -- and that has repeatedly eluded us over the past fifteen years -- is, I believe, now within our grasp. Whether or not it becomes a reality obviously does not depend exclusively on monetary policy, but the monetary actions taken in coming months and years will be critically important.

On the one hand, another prolonged period of restricted money growth as we had in 1981 and early 1982, would depress economic activity and would likely interrupt, if not prevent, the recovery. On the other hand, attempts to use excessive money growth as an economic stimulus carry a significant risk of back-firing. The key is money growth that is supportive of economic expansion, but not so stimulative that inflationary expectations move adversely. These expectations, which are already sensitized by the projected budget deficits, are the major factors that have held up long-term interest rates even as the actual rate of inflation has declined.

The immediate contribution that monetary policy can make to a sustainable economic expansion is to facilitate continued downward adjustment of price expectations, to allow the entire structure of interest rates to fall. Downward adjustment of longterm price expectations over the course of this year is necessary to assure a meaningful and lasting decrease in the cost of credit, which is a vital element to meaningful economic recovery. Holding short-term interest rates down by continuing to provide more reserves to the banking system, however, is not likely to produce the desired downward pressures on longer term interest rates.

The risk of excessive monetary expansion early in 1983 is <u>not</u> an immediate resurgence of inflation. It is unlikely that excessive money growth would have an appreciable effect on the price indices for more than a year. Instead, the danger comes from the potential impact of expectations about the longer term prospects for inflation.

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REPRESENTATIVE SHORT-TERM AND LONG-TERM INTEREST RATES

(weekly averages, January 1982 to February 11, 1983)

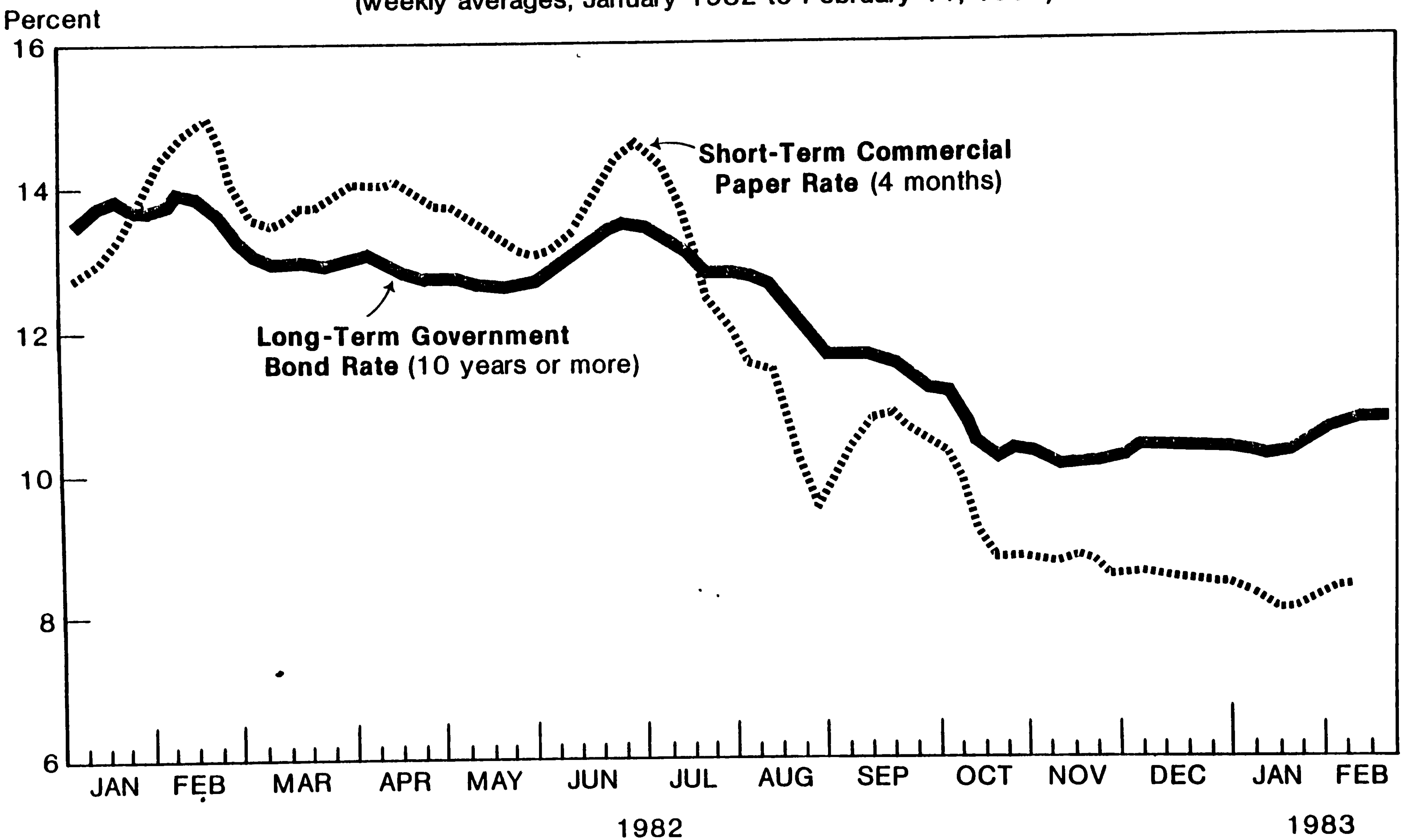
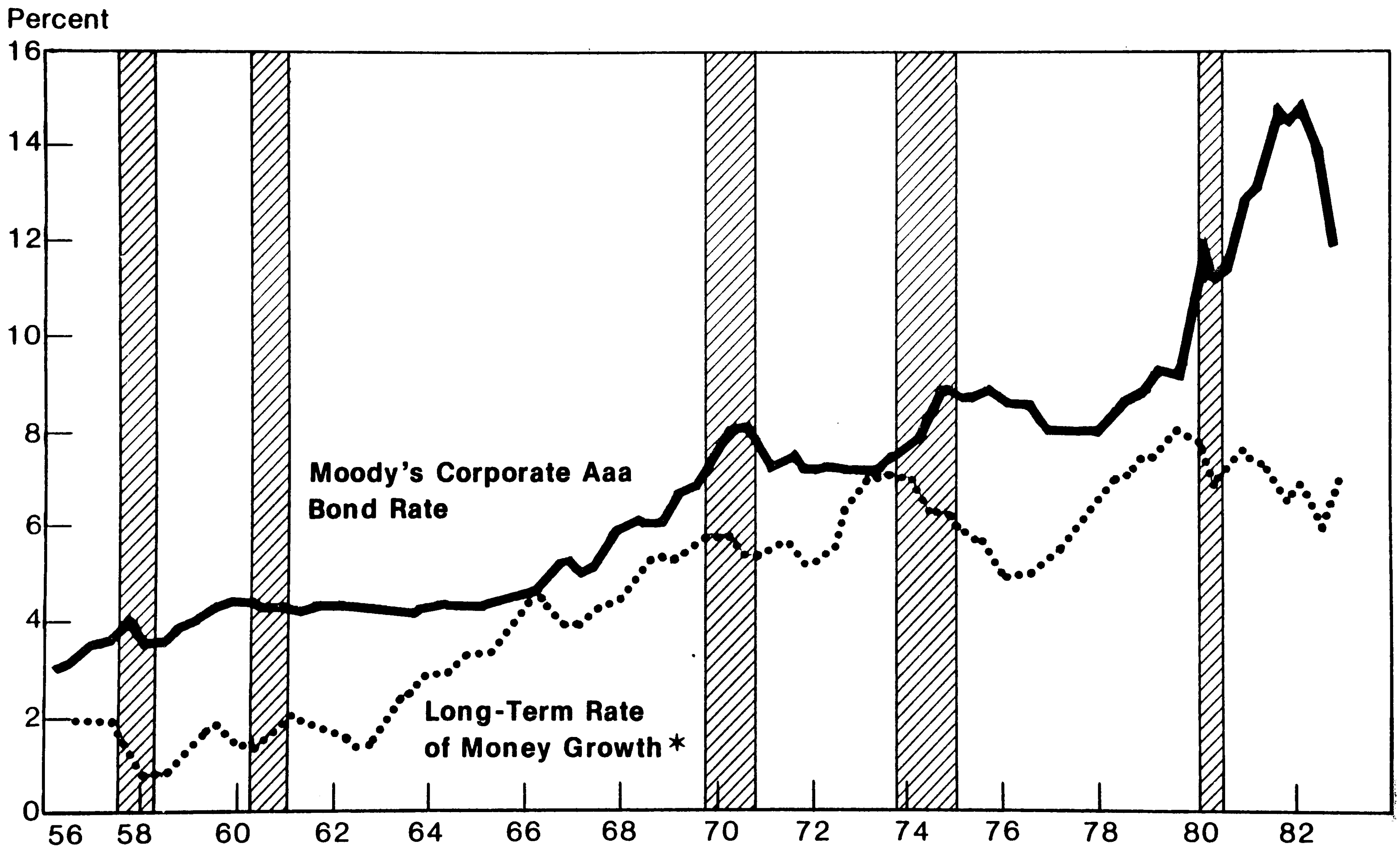


Chart 2

LONG-TERM MONEY GROWTH AND INTEREST RATES



*Money Growth is the rate of change in M1 over three years, expressed as an annual rate.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. February 22, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $ 12,400 million, to be issued March 3, 1983. This offering will provide $1,075 million of new cash for the Treasury, as the maturing bills are outstanding in the amount of $ 11,328 million, including $1,164 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and $ 2,226 million currently held by Federal Reserve Banks for their own account. The two series offered are as follows:

91 -day bills (to maturity date) for approximately $6,200 million, representing an additional amount of bills dated December 2, 1982, and to mature June 2, 1983 (CUSIP No. 912794 CW 2), currently outstanding in the amount of $5,812 million, the additional and original bills to be freely interchangeable.

182-day bills for approximately $ 6,200 million, to be dated March 3, 1983, and to mature September 1, 1983 (CUSIP No. 912794 DP 6).

Both series of bills will be issued for cash and in exchange for Treasury bills maturing March 3, 1983. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

R-2042

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, February 28, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on March 3, 1983, in cash or other immediately-available funds or in Treasury bills maturing March 3, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE February 22, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $6,201 million of 13-week bills and for $6,201 million of 26-week bills, both to be issued on February 24, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing May 26, 1983			:	26-week bills maturing August 25, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	98.028	7.801%	8.07%	:	95.983	7.946%	8.39%
Low	97.998	7.920%	8.19%	:	95.961	7.989%	8.44%
Average	98.006	7.888%	8.16%	:	95.969	7.973% 2/	8.42%

Tenders at the low price for the 13-week bills were allotted 89%.
Tenders at the low price for the 26-week bills were allotted 04%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 66,780	$ 66,780	:	$ 79,690	$ 38,010
New York	10,166,125	4,701,425	:	13,275,670	4,781,180
Philadelphia	32,040	32,040	:	15,935	15,935
Cleveland	87,055	71,505	:	44,395	34,395
Richmond	37,845	37,845	:	105,510	54,010
Atlanta	65,165	65,165	:	42,870	39,370
Chicago	1,020,875	585,025	:	749,265	106,375
St. Louis	37,770	31,770	:	63,840	52,840
Minneapolis	12,480	12,480	:	15,040	13,040
Kansas City	47,465	47,465	:	54,500	52,635
Dallas	29,700	29,700	:	21,170	16,170
San Francisco	745,030	261,730	:	1,362,705	766,705
Treasury	258,410	258,410	:	230,235	230,235
TOTALS	$12,606,740	$6,201,340	:	$16,060,825	$6,200,900
Type					
Competitive	$10,506,450	$4,101,050	:	$13,914,585	$4,054,660
Noncompetitive	1,030,800	1,030,800	:	770,240	770,240
Subtotal, Public	$11,537,250	$5,131,850	:	$14,684,825	$4,824,900
Federal Reserve	1,047,490	1,047,490	:	1,025,000	1,025,000
Foreign Official Institutions	22,000	22,000	:	351,000	351,000
TOTALS	$12,606,740	$6,201,340	:	$16,060,825	$6,200,900

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 8.233%.

R-2043

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-204

FOR IMMEDIATE RELEASE
February 22, 1983

CONTACT: Robert E. Nipp
(202) 566-2133

ROBERT J. LEUVER APPOINTED DIRECTOR OF TREASURY'S BUREAU OF ENGRAVING AND PRINTING

Secretary of the Treasury Donald T. Regan today announced the appointment of Robert J. Leuver as Director of the Bureau of Engraving and Printing. The appointment, effective immediately, fills a vacancy created when Harry R. Clements, the former director, resigned in early January to return to the private sector.

Mr. Leuver has most recently been Deputy Director and Assistant Director (Administration) at the Bureau. He has broad experience in organization, financial systems, information management, and general administration.

As Director of the Bureau of Engraving and Printing, Mr. Leuver is responsible for administering the world's largest security printing facility. The Bureau has annual sales in excess of $156 million and produces U.S. currency and postage stamps, public debt securities, and some 700 other miscellaneous security documents. It operates without an appropriation under a revolving fund. Public Law requires the Bureau to function economically and competitively. The Bureau employs 2,300 employees, all in Washington, D.C.

Before joining the Bureau in April 1979, Mr. Leuver worked five years in the Office of the Secretary as Chief, Treasury Employee Data and Payroll Division, and Program Manager for Management Information Systems. He served two years with ACTION, the parent agency for the Peace Corps, as Chief, Planning Division, and Chief, Management Analysis Staff.

Mr. Leuver was Executive Vice President, Claretians, Inc., for four years, and financial officer for 14 years. He also has served as a consultant to foreign countries and as a teacher and lecturer at colleges and universities.

A native of Chicago, Mr. Leuver, age 56, is married to the former Hilda Ortiz, also of Chicago. He graduated from Loyola University at Los Angeles with majors in Philosophy and English and has a Masters Degree from Catholic University of America, Washington, D.C.

R-2044

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TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

For Release Upon Delivery
Expected at 10 a.m. EST
February 23, 1983

STATEMENT OF
THE HONORABLE JOHN E. CHAPOTON
ASSISTANT SECRETARY
(TAX POLICY)
DEPARTMENT OF THE TREASURY
BEFORE THE
SUBCOMMITTEE ON SELECT REVENUE MEASURES
OF THE
HOUSE COMMITTEE ON WAYS AND MEANS

Mr. Chairman and Members of the Subcommittee:

I am pleased to have the opportunity to present the views of the Treasury Department on H.R. 1296, which deals with the tax treatment of farmers who participate in the Administration's Payment-in-Kind (PIK) program. Although we have some technical comments on the bill as currently drafted, the Treasury Department strongly supports legislation which would remove any disincentives in current tax law to farmers' participation in the PIK program.

BACKGROUND

The PIK program is a land diversion program designed to reduce the amount of certain agricultural commodities in the marketplace, thereby raising the prices of such commodities. Under the PIK program, the Department of Agriculture will compensate a participating farmer for removing acreage from active production by giving the farmer a percentage of the amount of the commodity he otherwise could have grown. The commodity is to be available to the farmer at the time of normal harvest, although the government will pay storage costs for up to five additional months.

Income Tax Consequences

Under current income tax law, a farmer would realize gross income from this transaction equal to the amount of the fair market value of the commodity received at the time the commodity is made available to him. The farmer would take a tax basis in the commodity equal to the amount included in income. He would recognize additional income (or loss) from the sale of the commodity if the amount realized from such sale exceeds (or is less than) the amount already included in income. Further, the farmer would be entitled to deduct his basis in the commodity to the extent it is used for feed.

The current law income tax treatment of the transaction involved in the PIK program is more complicated in the case of farmers who have nonrecourse loans outstanding from the Commodity Credit Corporation (CCC) secured by commodities which they either store on their own premises or in warehouses. The Department of Agriculture proposes to implement the PIK program for these farmers in two steps, as follows:

(1) the CCC will purchase the commodity from the farmer for an amount equal to the outstanding loan which is secured by the commodity, and the loan will thereby be discharged; and

(2) the CCC will then deliver that exact commodity or, in the case of farmers whose commodities are stored in warehouses, the warehouse receipt representing the commodity, to the farmer as his payment-in-kind under the PIK program.

The income tax consequences to a farmer in these circumstances would depend upon whether the farmer has made an election under section 77 of the Internal Revenue Code to treat the nonrecourse loan from the CCC as a sale for tax purposes. If the farmer makes a section 77 election, the loan proceeds are included in the farmer's income in the year of receipt. Since a farmer who has made a section 77 election has already been taxed on the proceeds of his CCC loan, the cancellation of that loan in exchange for the commodity securing the loan would have no further tax consequences to the farmer. The subsequent transfer of the commodity back to the farmer would be subject to the same tax treatment as described above; that is, the farmer would have gross income equal to the fair market value of the commodity when it is made available to him and would take a basis in the commodity equal to that value.

In the case of farmers who do not make a section 77 election, the CCC loan, when made, is treated as a loan rather than a sale. Therefore, the PIK transaction would be treated as a sale of the commodity for an amount equal to the outstanding debt which the commodity secured, followed by receipt of the commodity as a PIK payment. The result would be that the farmer would be taxed first on the amount of the debt which was discharged in the sale transaction and second on the amount of the fair market value of the commodity received in the PIK transaction. However, as discussed above, the farmer would take a basis in the commodity received equal to its value.

Estate Tax Consequences

Under section 2032A of the Internal Revenue Code, if certain requirements are met, real property which is used as a family farm and which passes to or is acquired by a qualified heir may be included in a decedent's estate at its current use value, rather than its full fair market value. Among the requirements which must be satisfied are: (1) the property must have been owned by the decedent or a member of his family and used "as a farm for farming purposes" on the date of the decedent's death and for periods aggregating five years or more during the eight-year period ending with the decedent's death; and (2) there must have been "material participation" in the operation of the farm by the decedent or a member of his family for periods aggregating five years or more out of the eight-year period ending on the date of the decedent's death.

Section 2032A also provides that the estate tax benefit of special use valuation generally is recaptured if the qualified heir disposes of the property to a nonfamily member or ceases to use the property "as a farm for farming purposes" within 10 years after the decedent's death and before the qualified heir's death. With certain exceptions, the qualified heir ceases to use the property for the qualified farming use if he or members of his family fail to participate materially in the farm operation for periods aggregating more than three years during any eight-year period ending after the decedent's death and before the qualified heir's death.

Another estate tax provision relevant to many farmers participating in the PIK program is section 6166 of the Code, which allows deferred payment of estate tax attributable to qualifying closely held business interests owned by decedents. The benefits of section 6166 are limited to interests in active trades or businesses.

A question may arise whether property on which a cash crop is not being grown as a result of participation in the PIK program, or in some other acreage-reduction program sponsored by the Department of Agriculture, is nevertheless being used "as a farm for farming purposes" within the meaning of section 2032A. Similar questions may be posed as to whether there has been the requisite "material participation" for purposes of section 2032A and whether the property is part of an active trade or business qualifying for estate tax deferral under section 6166.

None of these estate tax questions is specifically addressed in the present statute, and neither the regulations nor the published rulings have addressed these exact issues. It is Treasury's view, however, that the dedication of land to an acreage-reduction program sponsored by the Department of Agriculture generally should not prevent satisfaction of the requirements of section 2032A or section 6166 under present law, particularly where a portion of the farm remains in active production. In such a case, there would still be property used as a farm for farming purposes and material participation in its operation. Moreover, nothing in section 2032A or section 6166 requires that its tests be applied on an acre-by-acre basis. The fact that a portion of a farm is temporarily left fallow or covered with a conservation crop pursuant to an agreement with the Department of Agriculture does not mean that such portion is no longer a part of the farm or that it is not being used for farming purposes. In fact, fields are often temporarily removed from active production for soil conservation or other farming reasons having nothing to do with Federal acreage-reduction programs.

If a farmer removes his whole farm from active production, however, the result is somewhat less clear. In particular, if no portion of the farm is being used for farming purposes in the traditional sense, it is unclear whether there can be the required material participation in a farming operation. Also, it may be argued that if an entire farm is withdrawn from production, it has ceased to be used as a farm during that period.

DESCRIPTION OF H.R. 1296

Income Tax Provisions

H.R. 1296 would amend section 451 of the Code, which relates to the taxable year income is to be taken into account for tax purposes, by providing that a taxpayer may elect to exclude the value of commodities received under the PIK program from income in the year of receipt and to treat the commodities as if they were grown by him. Any commodities with respect to which such an election is made would have a zero basis for tax purposes. Thus, the farmer would realize income only at the time he sells the commodities or, if he uses the commodities for livestock feed, at the time he sells the livestock to which the commodities were fed.

Further, the bill would provide that taxpayers who would otherwise have to recognize income by reason of the cancellation of a CCC loan may elect to defer such income recognition. Under this election, a portion of the total proceeds from the cancelled loan would be included in income in the year the loan is cancelled and in succeeding taxable years in an amount equal to the proportion of the total commodity which secured the loan that is sold or consumed in each such taxable year.

Taxpayers may make either or both of the elections provided by H.R. 1296 separately with respect to each PIK payment received and each loan cancelled under the program.

Estate Tax Provisions

H.R. 1296 also would amend section 2032A to provide that the fact that property is removed from production pursuant to a "qualified Federal farmland removal program," shall not prevent (i) such property from being treated as used as a farm for farming purposes nor (ii) any individual from materially participating in the operation of the farm with respect to any property. A "qualified Federal farmland removal program" is any Federal program for removing land from agricultural production, including (but not limited to) the PIK program.

H.R. 1296 does not contain any provision which specifically addresses the effect of the PIK program on section 6166.

DISCUSSION

Timing of Income Recognition

Many farmers participating in the PIK program will have sold crops in the current taxable year which were harvested in a prior taxable year. Current law may impose a hardship on these taxpayers because they will have, in effect, income from two crops (the income from the prior year's crop that is sold, plus the income from the PIK payment) in the same taxable year. In addition, farmers participating in the PIK program will be under pressure to sell commodities to obtain cash to pay their income tax liabilities arising from the actual or constructive receipt of the PIK payments; and those sales may have to be made in a market flooded with commodities being sold by other farmers facing the same tax liquidity problem. These tax-motivated sales may cause farm commodity market problems of the type that the PIK program is designed to reduce. The potential tax and market problems also may discourage farmers from participating in the PIK program, thus frustrating Federal agricultural policy.

In view of these problems, the Treasury Department strongly supports changes in the current law which adopt the general policy position underlying H.R. 1296. Because PIK payments, in effect, are replacements for the commodities which farmers could have been expected to produce from the normal use of land devoted to the program, the tax law should treat farmers who receive commodities under the program as if they had grown the commodities themselves. Under this approach, farmers would recognize income only in the year they actually sell or otherwise dispose of the commodities in question. However, as I indicated earlier, we do have some technical comments on the bill as currently drafted.

First, we do not believe that the bill should be drafted as an amendment to section 451 of the Code. Section 451 relates to the timing of the recognition of income depending upon the taxpayer's method of accounting. Under either the cash or accrual method of accounting, a PIK payment would be recognized for tax purposes in the year the farmer receives or has a right to receive the payment. The issue is not one of timing but one of income inclusion. We believe that the bill should be drafted to provide an exclusion from gross income for commodities received under the PIK program and, further, to provide that those commodities will have a zero basis for income tax purposes.

Second, the bill would permit farmers who have not made a section 77 election to take any amounts realized from the CCC loans into income as the commodities are sold or consumed, rather than at the time the loans are discharged. We seriously question whether such relief is warranted. In such cases, the farmers already have received the cash necessary to pay any tax resulting from the income realized from the loan proceeds. Further, this provision of the bill would provide farmers who have not made a section 77 election with a significant advantage over those farmers who have made an election and have already paid tax on the loan proceeds received.

Third, we believe that the income tax rules provided by the bill should be mandatory rather than elective. Mandatory rules would be fully consistent with the objective of treating farmers who participate in and receive commodities under the PIK program as if they had grown the commodities themselves. We acknowledge that some taxpayers may have made the decision to enter into contracts with the Department of Agriculture based on the tax consequences under current law. If such taxpayers want taxable income during the current taxable year, however, they generally can achieve that result by selling the commodities received pursuant to the program in the current taxable year.

Special Use Valuation

Treasury generally supports the provisions of H.R. 1296 relating to section 2032A of the Code. To the extent that present law is unclear, these provisions will assure farmers that participation in the PIK program will not adversely affect their eligibility for special use valuation. Moreover, the provisions in H.R. 1296 dealing with section 2032A are consistent with the general approach of treating farmers as if they had grown the PIK commodities on the land they dedicate to the program.

Other Tax Consequences

The questions whether PIK payments should be treated as if farmers had grown the commodities themselves and whether farmers who divert some or all of their acreage under the PIK program should be considered as engaged in the trade or business of farming are questions that have ramifications for a number of other provisions of the Code. For instance, section 447 provides special accounting rules for corporations engaged in the trade or business of farming. Section 175 provides special treatment for soil and water conservation expenditures for taxpayers engaged in farming. Tax exempt farmers' cooperatives could lose their exemptions if the commodities received by their members and assigned to the cooperatives were not treated as produced by the members. Moreover, a determination of the self-employment income of a farmer who diverts acreage pursuant to the PIK program also depends on whether the farmer is deemed to participate materially in the production of farming commodities or the management of that production. Finally, a decedent's eligibility for estate tax deferral under section 6166 could be threatened if property involved in the PIK program is not treated as being used in an active trade or business. H.R. 1296 does not deal with any of these ancillary issues.

We believe that farmers who receive PIK payments should be treated as if they had grown the commodities received for all purposes of the Code and that participation in a Department of Agriculture program should be treated as a farming activity. We believe this result can be reached in most cases under current law. However, the legislation should address these ancillary issues to the extent that current law needs to be clarified to ensure appropriate results.

CONCLUSION

In conclusion, I would like to reiterate our strong support of legislation that will remove any impediment to the successful operation of the PIK program which current tax law may create. While I have noted some technical comments on the bill as currently drafted, I am confident that we can work out a satisfactory solution to these problems with the Subcommittee.

I would be happy to answer your questions.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

STATEMENT OF THE HONORABLE DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
SENATE COMMITTEE ON FOREIGN RELATIONS
Washington, D.C.
February 23, 1983

IMF Resources, World Financial Stability, and U.S. Interests

Mr. Chairman and members of the Committee:

It is a pleasure to appear before you today to explain and support the Administration's proposals for legislation to increase the resources of the International Monetary Fund. As you have requested, I will also discuss our proposals for the multilateral development banks.

After extensive consultations and negotiations among IMF members, agreement was completed earlier this month on complementary measures to increase IMF resources: an increase in quotas, the IMF's basic source of financing; and an expansion of the IMF's General Arrangements to Borrow (GAB), for lending to the IMF on a contingency basis, if needed to deal with threats to the international monetary system. These must now be confirmed by member governments, involving Congressional authorization and appropriation in our case, in order to become effective. As background to the legislative proposals which we plan to submit formally to the Congress later this week, I would like to outline the problems facing the international financial system, the importance to the United States of an orderly resolution of those problems, and the key role the IMF must play in solving them.

The International Financial Problem

Since about the middle of last year, the international monetary system has been confronted with serious financial problems. Last fall the debt and liquidity problems of Argentina, Brazil, Mexico, and a growing list of other borrowers became front-page news -- and correctly so, since management of these problems is critical to our economic interests. The debts of many key countries became too large for them to continue to manage under present policies and world economic circumstances; lenders began to retrench sharply; and the borrowers have since been finding it difficult if not impossible to scrape together the money to meet upcoming debt payments and to pay for essential imports. As a result, the international financial and economic system is experiencing strains that are without precedent in the postwar era and which threaten to derail world economic recovery.

There is a natural tendency under such circumstances for financial contraction and protectionism -- reactions that were the very seeds of the depression of the 1930s. It was in response to those tendencies that the International Monetary Fund was created in the aftermath of World War II, largely at the initiative of the United States, to provide a cooperative mechanism and a financial backstop to prevent a recurrence of that slide into depression. If the IMF is to be able to continue in that rôle, it must have adequate resources.

The current problem did not arise overnight, but rather stems from the economic environment and policies pursued over the last two decades. Inflationary pressures began mounting during the 1960's, and were aggravated by the commodity boom of the early 1970's and the two oil shocks that followed. For most industrialized countries, the oil shocks led to a surge of imported inflation, worsening the already growing inflationary pressures; to large transfers of real income and wealth to oil exporting countries; and to deterioration of current account balances. For the oil-importing less developed countries -- the LDCs -- this same process was further compounded by their loss of export earnings when the commodity boom ended.

Rather than allowing their economies to adjust to the oil shocks, most governments tried to maintain real incomes through stimulative economic policies, and to protect jobs in uncompetitive industries through controls and subsidies. Inflationary policies did bring a short-run boost to real growth at times, but in the longer run they led to higher inflation, declining investment and productivity, and worsening prospects for real growth and employment.

Similarly, while these policies delayed economic adjustment somewhat, they could not put it off forever. In the meanwhile, the size of the adjustment needed was getting larger. Important regions remained dependent on industries whose competitive position was declining; inflation rates and budget deficits soared; and -- most pertinent to today's financial problems -- many oil importing countries experienced persistent, large current account deficits and unprecedented external borrowing requirements. Some oil-exporting countries also borrowed heavily abroad, in effect relying on increasing future oil revenues to finance ambitious development plans.

In the inflationary environment of the 1970's, it was fairly easy for most nations to borrow abroad, even in such large amounts, and their debts accumulated rapidly. Most of the increased foreign debt reflected borrowing from commercial banks in industrial countries. By mid-1982, the total foreign debt of non-OPEC developing countries was something over $500 billion -- more than five times the level of 1973. Of that total, roughly $270 billion was owed to commercial banks in the industrial countries, and more than half of that was owed by only three Latin American countries -- Argentina, Brazil, and Mexico. New net lending to non-OPEC LDCs by banks in the industrial countries grew at a rising pace -- about $37 billion in 1979, $43 billion in 1980, and $47 billion in 1981 -- with most of the increase continuing to go to Latin America. (See Charts A and B.)

That there has been inadequate adjustment and excessive borrowing has become painfully clear in the current economic environment -- one of stagnating world trade, disinflation, declining commodity prices, and interest rates which are still high by historical standards. Over the past two years, there has been a strong shift to anti-inflationary policies in most industrial countries, and this shift has had a major impact on market attitudes. Market participants are beginning to recognize that our governments intend to keep inflation under control in the future and are adjusting their behavior accordingly.

In most important respects, the impact of this change has been positive. Falling inflation expectations have led to major declines in interest rates. There has been a significant drop in the cost of imported oil. On the financial side, there is a shift toward greater scrutiny of foreign lending which may be positive for the longer run, even though there are short-term strains. Lenders are re-evaluating loan portfolios established under quite different expectations about future inflation. Levels of debt that were once expected to decline in real terms because of continued inflation -- and therefore to remain easy for borrowers to manage out of growing export revenues -- are now seen to be high in real terms and not so manageable in a disinflationary world. As a result, banks have become more cautious in their lending -- not just to LDCs but to domestic borrowers as well.

There is certainly nothing wrong with greater exercise of prudence and caution on the part of commercial banks -- far from it. Since banks have to live with the consequences of their decisions, sound lending judgment is crucial. In addition, greater scrutiny by lenders puts pressure on borrowers to improve their capacity to repay, and creates an additional incentive for borrowing countries to undertake needed adjustment measures.

But a serious short-run problem has arisen as a result of the size of the debt of several key countries, the turn in the world economic environment, inadequacy of adjustment policies, and the speed with which countries' access to external financing has been cut back. Last year, net new bank lending to non-OPEC LDCs dropped by roughly half, to something in the range of $20 to $25 billion for the year as a whole (Chart B), and came to a virtual standstill for a time at mid-year. This forced LDCs to try to cut back their trade and current account deficits sharply to match the reduced amount of available external financing.

The only fast way for these countries to reduce their deficits significantly in the face of an abrupt cutback in financing is to cut imports drastically, either by sharply depressing their economies to reduce demand or by restricting imports directly. Both of these are damaging to the borrowing countries, politically and socially disruptive, and painful to industrial economies like the United States -- because almost all of the reduction in LDC imports must come at the direct expense of exports from industrial countries.

But as the situation has developed in recent months, there has been a danger that lenders might move so far in the direction of caution that they compound the severe adjustment and liquidity problems already faced by major borrowers, and even push other countries which are now in reasonably decent shape into serious financing problems as well.

The question is one of the speed and degree of adjustment. While the developing countries must adjust their economies to reduce the pace of external borrowing and maintain their capacity to service debt, there is a limit, in both economic and political terms, to the speed with which major adjustments can be made. Effective and orderly adjustment takes time, and attempts to push it too rapidly can be destabilizing.

Importance to the United States of an Orderly Resolution

It is right for American citizens to ask why they and their government need be concerned about the international debt problem. Why should we worry if some foreign borrowers get cut off from bank loans? And why should we worry if banks lose money? Nobody forced them to lend, and they should live with the consequences of their own decisions like any other business.

If all the U.S. government had in mind was throwing money at the borrowers and their lenders, it would be difficult to justify using U.S. funds on any efforts to resolve the debt crisis, especially at a time of domestic spending adjustment.

But of course, there is more to the problem, and to the solution. First, a further abrupt and large-scale contraction of LDC imports would do major damage to the U.S. economy. Second, if the situation were handled badly, the difficulties facing LDC borrowers might come to appear so hopeless that they would be tempted to take desperate steps to try to escape. The present situation is manageable. But a downward spiral of world trade and billions of dollars in simultaneous loan losses would pose a fundamental threat to the international economic system, and to the American economy as well.

In order to appreciate fully the potential impact on the U.S. economy of rapid cutbacks in LDC imports, it is useful to look at how important international trade has become to us. Trade was the fastest growing part of the world economy in the last decade -- but the volume of U.S. exports grew even faster in the last part of the 1970's, more than twice as fast as the volume of total world exports. By 1980, nearly 20 percent of total U.S. production of goods was being exported, up from 9 percent in 1970, although the proportion has fallen slightly since then. (Charts C and D.)

Among the most dynamic export sectors for this country are agriculture, services, high technology, crude materials and fuels. American agriculture is heavily export-oriented: one in three acres of U.S. agricultural land, and 40 percent of agricultural production, go to exports. This is one sector in which we run a consistent trade surplus, a surplus that grew from $1.6 billion in 1970 to over $24 billion in 1980. (Chart E.)

Services trade -- for example, shipping, tourism, earnings on foreign direct investment and lending -- is another big U.S. growth area. The U.S. surplus on services trade grew from $3 billion in 1970 to $34 billion in 1980, and has widened further since. (Chart F.) When both goods and services are combined, it is estimated that one-third of U.S. corporate profits derive from international activities.

High technology manufactured goods are a leading edge of the American economy, and not surprisingly net exports of these goods have grown in importance. The surplus in trade in these products rose from $7.6 billion in 1970 to $30 billion in 1980. And even in a sector we do not always think of as dynamic -- crude materials and non-petroleum fuels like coal -- net exports rose six-fold, from $2.4 billion to $14.6 billion over the same period.

Vigorous expansion of our export sectors has become critical to employment in the United States. (Chart G.) The absolute importance of exports is large enough -- they accounted directly for 5 million jobs in 1982, including one out of every eight jobs in manufacturing industry. But export-related jobs have been getting even <u>more</u> important at the margin. A survey in the late 1970s indicated that four out of every five <u>new</u> jobs in U.S. manufacturing was coming from foreign trade; on average, it is estimated that every $1 billion increase in our exports results in 24,000 new jobs. Later I will detail how Mexican debt problems have caused a $10 billion annual-rate drop in our exports to Mexico between the end of 1981 and the end of 1982. By the rule of thumb I just gave, that alone -- if sustained -- would mean the loss of a quarter of a million American jobs.

These figures serve to illustrate the overall importance of exports to the U.S. economy. The story can be taken one step further, to relate it more closely to the present financial situation. Our trading relations with the non-OPEC LDCs have expanded even more rapidly than our overall trade. Our exports to the LDCs, which accounted for about 25 percent of total U.S. exports in 1970, rose to about 29 percent by 1980. (Chart H.) In manufactured goods, which make up two-thirds of our exports, the share going to LDCs rose even more strongly -- from 29 percent to 39 percent. In fact, since the mid-1970's trade with LDCs has accounted for more than half of the overall growth of American exports.

What these figures mean is that the export sector of our economy -- a leader in creating new jobs -- is tremendously vulnerable to any sharp cutbacks in imports by the non-OPEC LDCs. Yet that is exactly the response to which debt and liquidity problems have been driving them. This is a matter of concern not just to the banking system, but to American workers, farmers, manufacturers and investors as well.

Even on the banking side, there are indirect impacts of concern to all Americans. A squeeze on earnings and capital positions from losses on foreign loans not only would impair banks' ability to finance world trade, but also could ultimately mushroom into a significant reduction in their ability to lend to domestic customers and an increase in the cost of that lending.

Beyond our obvious interest in maintaining world trade and trade finance, there is another less-recognized U.S. financial interest. The U.S. government faces a potential exposure through Federal lending programs administered by Eximbank and the Commodity Credit Corporation. This exposure -- built in support of U.S. export expansion -- amounted to $35 billion at the end of 1982, including $24 billion of direct credits (mostly from Eximbank) and $11 billion of guarantees and insurance. Argentina, Brazil and Mexico are high on the list of borrowers. Should loans extended or guaranteed under these programs sour, the U.S. Treasury -- meaning the U.S. taxpayer -- would be left with the loss. We have a direct interest in avoiding this addition to Federal financing requirements.

All industrial economies, including the American economy, will inevitably bear some of the costs of the balance of payments adjustments LDCs must make and are already making. This adjustment would be much deeper, for both the borrowing countries and for lending countries like the United States, if banks were to pull back entirely from new lending this year. In 1983, for example, a flat standstill would require borrowers to make yet another $20 to $25 billion cut in their trade and current account deficits, which would be considerably harder to manage if it came right on the heels of similar cuts they have already made. Further adjustments are needed -- but again the question is one of the size and speed of adjustment. If these countries were somehow to make adjustments of that size for a second consecutive year, the United States and other industrial countries would then have to suffer large export losses once again. At the early stages of U.S. and world economic recovery we are likely to be in this year, a drop in export production of this size could abort the gradual rebuilding of consumer and investor confidence we need for a sustained recovery.

In fact, many borrowers have already taken very difficult adjustment measures to get this far. If they were forced to contemplate a second year of further massive cutbacks in available financing, they could be driven to consider other measures to reduce the burden of their debts. Here potentially lies a still greater threat to the financial system.

When interest payments are more than 90 days late, not only are bank profits reduced by the lost interest income, but they may also have to begin setting aside precautionary reserves to cover potential loan losses. If the situation persisted long enough, the capital of some banks might be reduced.

Banks are required to maintain an adequate ratio between their underlying capital and their assets -- which consist mainly of loans. For some, shrinkage of their capital base would force them to cut back on their assets -- meaning their outstanding loans -- or at least on the growth of their assets -- meaning their new lending. Banks would thus be forced to make fewer loans to all borrowers, domestic and foreign, and they would also be unable to make as many investments in securities such as municipal bonds. Reduced access to bank financing would thus force a cutback in the expenditures which private corporations and local governments can make -- and it would also put upward pressure on interest rates.

The usual perception of international lending is that it involves only a few large banks in the big cities, concentrated in half a dozen states. The facts are quite different. We have reliable information from bank regulatory agencies and Treasury reports identifying nearly 400 banks in 35 states and Puerto Rico that have foreign lending exposures of over $10 million -- and in all likelihood there are hundreds more banks with exposures below that threshhold but still big enough to make a significant dent in their capital and their ability to make new loans here at home. Banks in most states are involved, and the more abruptly new lending to troubled borrowing countries is cut back, the more likely it is that the fallout from their problems will feed back back on the U.S. financial system and weaken our economy. Many U.S. corporations also have claims on foreign countries, related to their exports and foreign investments.

Resolving the International Financial Problem

Debt and liquidity problems did not come into being overnight, and a lasting solution will also take some time to put into place. We have been working on a broad-based strategy involving all the key players -- LDC governments, governments in the industrialized countries, commercial banks, and the International Monetary Fund. This strategy has five main parts:

First, and in the long run most important, must be effective adjustment in borrowing countries. In other words, they must take steps to get their economies back on a stable course, and to make sure that imports do not grow faster than their ability to pay for them. Each of these countries is in a different situation, and each faces its own unique constraints. But in general, orderly and effective adjustment will not come overnight. The adjustment will have to come more slowly, and must involve expansion of productive investment and exports. In many cases it will entail multi-year efforts, usually involving measures to address some combination of the following problems: rigid exchange rates; subsidies and protectionism; distorted prices; inefficient state enterprises; uncontrolled government expenditures and large fiscal deficits; excessive and inflationary money growth; and interest rate controls which discourage private savings and distort investment patterns. The need for such corrective policies is recognized, and being acted on, by major borrowers -- with the support and assistance of the IMF.

The second element in our overall strategy is the continued availability of official balance of payments financing, on a scale sufficient to help see troubled borrowers through the adjustment period. The key institution for this purpose is the International Monetary Fund. The IMF not only provides temporary balance of payments financing, but also ensures that use of its funds is tied tightly to implementation of needed policy measures by borrowers.

It is this aspect -- IMF conditionality -- that makes the role of the IMF in resolving the current debt situation and the adequacy of its resources so important.

IMF resources are derived mainly from members' quota subscriptions, supplemented at times by borrowing from official sources. Assessing the adequacy of these resources over any extended period is extremely difficult and subject to wide margins of error. The potential needs for temporary balance of payments financing depend on a number of variables, including members' current and prospective balance of payments positions, the availability of other sources of financing, the strength of the conditionality associated with the use of IMF resources, and members' willingness and ability to implement the conditions of IMF programs. At the same time, the amount of IMF resources that is effectively available to meet its members' needs at any point in time depends not only on the size of quotas and borrowing arrangements, but also on the currency composition of those resources in relation to balance of payments patterns, and on the amount of members' liquid claims on the IMF which might be drawn. In view of all these variables, assessments of the IMF's "liquidity" -- its ability to meet members' requests for drawings -- can change very quickly.

Still, as difficult as it is to judge the adequacy of IMF resources in precise terms, most factors point in the same direction at present. The resources now effectively available to the IMF have fallen to very low levels in absolute terms, in relation to broad economic aggregates such as world trade, and in relation to actual and potential use of the IMF.

At the beginning of this year, the IMF had about SDR 28 billion available for lending. However, SDR 19 billion of that total had already been committed under existing IMF programs or was expected to be committed shortly to programs already negotiated, leaving only about SDR 9 billion available for new commitments. Given the scope of today's financing problems, requests for IMF programs by many more countries must be anticipated over the next year, and it is probable that unless action is taken to increase IMF resources its ability to commit funds to future adjustment programs will be exhausted by late 1983 or early 1984. I will return to our specific proposals in this area shortly.

The IMF cannot be our only buffer in financial emergencies. It takes time for borrowers to design and negotiate lending programs with the IMF and to develop financing arrangements with other creditors. As we have seen in recent cases, the problems of troubled borrowers can sometimes crystallize too quickly for that process to reach its conclusion -- in fact, the real liquidity crunch came in the Mexican and Brazilian cases before such negotiations even started.

Thus, the third element in our strategy is the willingness of governments and central banks in lending countries to act quickly to respond to debt emergencies when they occur. Recent experience has demonstrated the need to consider providing immediate and substantial short-term financing -- on a selective basis, where system-wide dangers are present -- to tide countries through their negotiations with the IMF and discussions with other creditors.

We are undertaking this where necessary, on a case-by-case basis, through ad hoc arrangements among finance ministries and central banks, often in cooperation with the Bank for International Settlements. But it must be emphasized that these lending packages are short-term in nature, designed to last for only a year at most and normally much less, and cannot substitute for IMF resources which are designed to help countries through a multi-year adjustment process.

In fact, IMF resources themselves have only a transitional and supporting role. The overall amount of Fund resources, while substantial, is limited and not in any event adequate to finance all the needs of its members. While we feel that a sizeable increase in IMF resources is essential, this increase is not a substitute for lending by commercial banks. Private banks have been the largest single source of international financing in the past to both industrial and developing countries, and this will have to be the case in the future as well -- including during the crucial period of adjustment.

Thus, the fourth essential element in resolving debt problems is continued commercial bank lending to countries that are pursuing sound adjustment programs. In the last months of 1982 some banks, both in United States and abroad, sought to limit or reduce outstanding loans to troubled borrowers. But an orderly resolution of the present situation requires not only a willingness by banks to "roll over" or restructure existing debts, but also to increase their net lending to developing countries, including the most troubled borrowers, to support effective, non-disruptive adjustment. The increase in net new commercial bank lending needed for just three countries -- Brazil, Argentina, and Mexico -- will approach $11 billion in 1983. Without this continued lending in support of orderly and constructive economic adjustment, the programs that have been formulated with the IMF cannot succeed -- and the lenders have a strong self-interest in helping to assure success. It should be noted, however, that new bank lending will be at a slower rate than that which has characterized the last few years -- more in line with the increase in 1982 than what we saw in 1980 or 1981.

The final part of our strategy is to restore sustainable economic growth and to preserve and strengthen the free trading system. The world economy is poised for a sustained recovery: inflation rates in most major countries have receded; nominal interest rates have fallen sharply; inventory rundowns are largely complete.

Solid, observable U.S. recovery is one critical ingredient missing for world economic expansion. We believe the U.S. recovery is now getting underway, as evidenced by the recent drop in unemployment and upturns in orders and production. Establishing credible growth in other industrial economies is also important and we believe the base for recovery is being laid abroad as well.

However, both we and others must exercise caution at this turning point. Governments must not give in to political pressures to stimulate their economies too quickly through excessive monetary or fiscal expansion. A major shift at this stage could place renewed upward pressure on inflation and interest rates.

In addition, rising protectionist pressures, both in the United States and elsewhere, pose a real threat to global recovery and to the resolution of the debt problem. When one country takes protectionist measures hoping to capture more than its fair share of world trade, other countries will retaliate. The result is that world trade shrinks, and rather than any one country gaining additional jobs, everybody loses. More importantly for current debt problems, we must remember that export expansion by countries facing problems is crucial to their balance of payments adjustment efforts. Protectionism cuts off the major channel of such expansion. That adjustment is essential to restoring problem country debtors to sustainable balance of payments positions and avoiding further liquidity crises -- and as we have seen, it is therefore essential to the economic and financial health of the United States.

The only solution is a stronger effort to resist protectionism. As the world's largest trading nation, the United States carries a major responsibility to lead the world away from a possible trade war. The clearest and strongest signal for other countries would be for the United States to renounce protectionist pressures at home and to preserve its essentially free trade policies. That signal would be followed, and would reinforce, continued U.S. efforts to encourage others to open their markets, and would in turn be reinforced by IMF program requirements for less restrictive trade policies by borrowers.

The Role and Resources of the IMF

I have stressed the role of the International Monetary Fund in dealing with the current financial situation, and now I would like to expand on that point. The IMF is the central official international monetary institution, established to promote a cooperative and stable monetary framework for the world economy. As such, it performs many functions beyond the one we are most concerned with today -- that of providing temporary balance of payments financing in support of adjustment. These include monitoring the appropriateness of its members' foreign exchange arrangements and policies, examining their economic policies, reviewing the adequacy of international liquidity, and providing mechanisms through which its member governments cooperate to improve the functioning of the international monetary system.

In that context, it becomes clearer that IMF financing is provided only as part of its ongoing systemic responsibilities. Its loans to members are made on a temporary basis in order to safeguard the functioning of the world financial system -- in order to provide borrowers with an extra margin of time and money which they can use to bring their external positions back into reasonable balance in an orderly manner, without being forced into abrupt and more restrictive measures to limit imports. The conditionality attached to IMF lending is designed to assure that orderly adjustment takes place, that the borrower is restored to a position which will enable it to repay the IMF over the medium term. In addition, a borrower's agreement with the IMF on an economic program is usually viewed by financial market participants as an international "seal of approval" of the borrower's policies, and serves as a catalyst for additional private and official financing.

The money which the IMF has available to meet its members' temporary balance of payments financing needs comes from two sources: quota subscriptions and IMF borrowing from its members. The first source, quotas, represents the Fund's main resource base and presently totals some SDR 61 billion, or about $67 billion at current exchange rates. The IMF periodically reviews the adequacy of quotas in relation to the growth of international transactions, the size of likely payments imbalances and financing needs, and world economic prospects generally.

At the outset of the current quota discussions in 1981, many IMF member countries favored a doubling or tripling of quotas, arguing both that large payments imbalances were likely to continue and that the IMF should play a larger intermediary role in financing them. While agreeing that quotas should be adequate to meet prospective needs for temporary financing, the United States felt that effective stabilization and adjustment measures should lead to a moderation of payments imbalances, and that a massive quota increase was not warranted. Nor did we feel that an extremely large quota increase would be the most efficient way to equip the IMF to deal with unpredictable and potentially major financing problems that could threaten the stability of the system as a whole, and for which the IMF's regular resources were inadequate.

Accordingly, the United States proposed a dual approach to strengthening IMF resources:

-- First, a quota increase which, while smaller than many others had wanted, could be expected to position the IMF to meet members' needs for temporary financing in normal circumstances.

-- Second, establishment of a contingency borrowing arrangement that would be available to the IMF on a stand-by basis for use in situations threatening the stability of the system as a whole.

This approach has been adopted by the IMF membership, in agreements reached by the major countries in the Group of Ten in mid-January, and by all members at the IMF's Interim Committee meeting last week.

The agreed increase in IMF quotas is 47 percent, an increase from SDR 61 billion to SDR 90 billion (in current dollar terms, an increase from $67 billion to $99 billion). The proposed increase in the U.S. quota is SDR 5.3 billion ($5.8 billion at current exchange rates) representing 18 percent of the total increase.

The Group of Ten, working with the IMF's Executive Board, has agreed to an expansion of the IMF's General Arrangements to Borrow from the equivalent of about SDR 6.5 billion at present to a new total of SDR 17 billion, and to changes in the GAB to permit its use, under certain circumstances, to finance drawings on the IMF by any member country. Under this agreement, the U.S. commitment to the GAB would rise from $2 billion to SDR 4.25 billion, equivalent to an increase of roughly $2.6 billion at current exchange rates.

We believe this expansion and revision of the GAB offers several important attractions and, as a supplement to the IMF's quotas, greatly strengthens the IMF's role as a backstop to the system:

-- First, since GAB credit lines are primarily with countries that have relatively strong reserve and balance of payments positions, they can be expected to provide more effectively usable resources than a quota increase of comparable size. Consequently, expansion of the GAB is a more effective and efficient means of strengthening the IMF's ability to deal with extraordinary financial difficulties than a comparable increase in quotas.

-- Second, since the GAB will not be drawn upon in normal circumstances, this source of financing will be conserved for emergency situations. By demonstrating that the IMF is positioned to deal with severe systematic threats, an expanded GAB can provide the confidence to private markets that is needed to ensure that capital continues to flow, thus reducing the risk that the problems of one country will affect others.

-- And third, creditors under this arrangement will have to concur in decisions on its activation, ensuring that it will be used only in cases of systemic need and in support of effective adjustment efforts by borrowing countries.

Annex A to my statement contains the texts of the relevant Interim Committee and Group of Ten communiques. These substantive agreements will be codified in formal Governors and Executive Board decisions in the next few weeks. In sum, the proposed increase in U.S. commitments to the IMF totals SDR 7.7 billion -- SDR 5.3 billion for the increase in the U.S. quota and SDR 2.4 billion for the increase in the U.S. commitment under the GAB. At current exchange rates, the dollar equivalents are $8.4 billion in total, $5.8 billion for the quota increase and $2.6 billion for the GAB increase.

We believe these steps to strengthen the IMF, if enacted, will safeguard the IMF's ability to respond effectively to current financial problems. Given the financing needs we foresee, we feel it is important that the increases be implemented by the end of this year. Without such a timely and adequate increase in IMF resources, the ability of the monetary system to weather debt and liquidity problems will be impaired, at substantial direct and indirect cost to the United States.

The U.S. share in the increase in IMF resources is 18 percent, which obviously means other countries are putting up the remaining 82 percent, the great bulk of the increase. By putting up 18 percent of the increase, we will maintain our voting share at just over 19 percent. The principle of weighted voting on which the IMF operates has been key to its effectiveness over the years and to ensuring that we have a voice and vote comparable to the share of resources we provide. Major policy decisions -- such as those just taken on the quota increase -- require an 85 percent majority vote, giving us a veto over all such decisions. Some of our allies would claim that we aren't pulling our own weight -- that our stake in world trade and finance is bigger than the share of resources we are proposing to put into the IMF would indicate.

Political and Security Interests

While fundamentally the IMF is designed to further our economic interests, in so doing it also benefits U.S. political and security interests. The IMF is essentially a non-political institution, with membership open to any country judged willing and able to meet the obligations of membership. But it serves our interests well by containing economic problems which could otherwise spread through the international community; as a stabilizing element in countries facing the social and economic dislocations which can accompany adjustment; and supporting open, market-oriented economic systems consistent with Western political values. Judged on this criterion, U.S. appropriations for the IMF can be an excellent investment if they can help to avoid political upheaval in countries of critical interest to the United States.

I said earlier that the IMF was formed out of conviction that a cooperative institution was needed to help prevent a recurrence of the Great Depression of the 1930s. But that is only half the story. The other half is that the Western leaders who joined together in 1944 set up the Fund did so in recognition of the fact that the economic and financial disruptions of the 1930s had been a major cause of World War II. "Beggar thy neighbor" policies that try to shift the burden of adjustment to other countries inevitably heighten worldwide political tensions -- and these are the policies that the IMF is meant to avoid. As volatile as the world environment has been at times in the postwar era, on balance it has been a period of unprecedented prosperity, and the international tensions we have experienced could only have been worse without the IMF.

Some observers have suggested that Fund programs create political instability in countries which use conditional financing by forcing unpopular economic measures on them. The process of economic adjustment is rarely pleasant -- but as we have seen, economic adjustment has to come in any event, with or without an IMF program. Without a program, adjustment can be abrupt and destabilizing. By making the process more rational and orderly, the IMF can help countries avoid unnecessary sacrifices and thereby minimize threats to their political stability.

IMF programs, technical assistance, and general policy advice all help to support greater reliance on decentralized, market-oriented economic systems. In practice this translates into IMF support for the private sector, freer markets, the use of price signals, and a whole array of policies that strengthen the individual's opportunity and incentive to respond and shape economic developments. It is a central tenet of the American experience that this is a prerequisite for a strong democratic system. Over time, this approach helps to foster economic institutions and philosophies that are conducive to democratic values.

In testimony on security and economic assistance last week, Secretary Shultz made the point that by improving economic conditions abroad these U.S. appropriations could avoid the necessity of sending our military forces abroad more often. He noted that there have been 185 incidents since the end of World War II in which our forces were sent overseas to protect U.S. economic or political interests. I would not want to stretch this point too far in relation to the IMF -- but surely here, too, it has some validity. The greater economic stability and reliance on sound economic policies that the IMF fosters can reduce the potential for political disruption.

Concerns about the Increase in IMF Resources

The general outline of our proposals has been known to members of Congress for some time. Many have expressed reservations or questions about this proposal, and I would like to discuss some of the main concerns now.

- Is the IMF "Foreign Aid"?

Many perceive money appropriated for IMF use to be just another form of foreign aid, and question why we should be providing U.S. funds to foreign governments. Let me assure you that the IMF is not a development institution. It does not finance dams, agricultural cooperatives, or infrastructure projects. I have already made the point that the IMF is a monetary institution. Only one of its functions is providing balance of payments financing to its members in order to promote orderly functioning of the monetary system, and only then on a temporary basis, on medium-term maturities, after obtaining agreement to the fulfillment of policy conditions. We have been working very hard with the IMF to ensure that both the effectiveness of IMF policy conditions, and the temporary nature of its financing, are safeguarded. In this way, the Fund's financing facilities will continue to have a revolving nature and to promote adjustment.

IMF conditionality has been controversial over the years, with strong opinions on both sides. Some observers have worried that conditionality is so weak and ineffective that conditional lending is virtually a giveaway. Others believe that conditionality is too tight -- that it imposes unnecessary hardship on borrowers, and stifles economic growth and development.

Such generalizations reflect a misunderstanding of IMF conditionality. When providing temporary resources to a country faced with external financing problems, the IMF seeks to assure itself that the country is pursuing policies that will enable it to live within its means -- that is, within its ability to obtain foreign financial resources. It is this that determines the degree of adjustment that is necessary. It is often the case that appropriate economic policies will strengthen a country's borrowing capacity, and result in both higher import growth and higher export growth. I would cite the example of Mexico as an immediate case in point.

Mexico is our third largest trading partner, after Canada and Japan. And, as recently as 1981, it was a partner with whom we had an export boom and a substantial trade surplus, exporting goods to meet the demands of its rapidly growing population and developing economy. This situation changed dramatically in 1982, as Mexico began experiencing severe debt and liquidity problems. By late 1982, Mexico no longer had access to financing sufficient to maintain either its imports or its domestic economic activity. As a result, U.S. exports to Mexico dropped by a staggering 60 percent between the fourth quarter of 1981 and the fourth quarter of 1982. Were our exports to Mexico to stay at their depressed end-1982 levels, this would represent a $10 billion drop in exports exports to our third largest market in the world. Because the financing crunch got worse as the year wore on, totals for the full year 1982 don't tell the story quite so dramatically -- but even they are bad enough. Our $4 billion trade surplus surplus with Mexico in 1981 was transformed into a trade deficit of nearly $4 billion in 1982, due mainly to an annual-average drop in U.S. exports of one-third. (Chart I.) This $8 billion deterioration was our worst swing in trade performance with any country in the world, and it was due almost entirely to the financing problem.

We believe that now this situation will start to turn around, and we can begin to resume more normal exports to Mexico. If this happens, it will be due in large part to the fact that, late in December, an IMF program for Mexico went into effect; and that program is providing the basis not only for IMF financing, but for other official financing and for a resumption of commercial bank lending as well. Mexico must make difficult policy adjustments if it is to restore creditworthiness. The Mexican authorities realize this and are embarked on a courageous program. But the existence of IMF financing and the other financing associated with it will permit Mexico to resume something more like a normal level of economic activity and imports while the adjustment takes place in an orderly manner. Without the IMF program, all we could look forward to would be ever-deepening depression in Mexico and still further declines in our exports to that country.

There is another aspect of the distinction between IMF financing and foreign aid which we should be very clear on, since it goes to the heart of U.S. relations with the Fund. All IMF members provide financing to the IMF under their quota subscriptions, and all -- industrial and developing alike -- have the right to draw on the IMF. Quota subscriptions form a kind of revolving fund, to which all members contribute and from which all are potential borrowers.

As an illustration, in practice our quota subscription has been drawn upon many times -- and repaid -- over the years for lending to other IMF members. We in turn have drawn on the IMF on 24 occasions -- most recently in November 1978 -- and our total cumulative drawings, amounting to the equivalent of $6.5 billion, are the second largest of any member (the United Kingdom has been the largest user of IMF funds). (U.S. drawings on the IMF are described at Annex B.)

° Do IMF Programs Hurt U.S. Exports?

There is a widespread perception that IMF programs are designed to cut imports by countries which use IMF financing, and thus hurt U.S. exports to those countries. Some would argue, in fact, that far from helping to maintain world trade and U.S. exports, our participation in the increase in IMF resources would contribute to further reductions in our exports.

This is simply a misreading of the IMF. The whole point of an IMF program is to get a borrower's external balance back within sustainable limits -- but to judge the effects of those programs on our exports you always have to start by asking what would have happened without an IMF program. When a country draws on IMF financing, it usually does so in recognition of the fact that its external deficit is not going to be sustainable if it stays on its present course. If the borrower didn't go to the IMF, it would likely be cut off from further external financing from other sources and would have to cut back drastically on imports, as we saw in the case of Mexico.

Furthermore, IMF programs are not just directed at slowing the growth of imports. Reducing import growth is often one of the short-run priorities, but even then IMF financing can permit a higher level of imports than would otherwise be the case. And equally important are steps to increase a country's export capacity, thereby giving it the ability to pay for higher imports in the long run.

Exchange rate devaluations are often an important part of IMF programs -- devaluations intended to ensure that the right price signals are sent to domestic producers, importers and exporters, and that the competitiveness of domestic industries is restored. These devaluations have often been accompanied by the removal of restrictions on trade and capital flows. And, to lay one total misunderstanding to rest, an IMF program never calls for the tightening of import restrictions -- in fact, new or intensified restrictions are expressly prohibited. The IMF does not promote restrictions -- its purposes and policies go precisely in the opposite direction.

° Why Not Spend the Money at Home?

Another major concern with the proposals to increase IMF resources is that, in this period of budgetary stringency, many believe we would be better advised to spend the money at home. There is also some feeling that if we were to get the U.S. economy moving forward again, the international financial problem would take care of itself. I think I've already been through part of the response to these concerns when I described the large and growing impact which foreign trade now has on American growth and employment. We will do what is necessary domestically to strengthen our economy. But we will leave a major threat to domestic recovery unaddressed if we do not act to resolve the international financial situation. The direct impact alone of international developments on our economy is so large that, were the international situation not to improve, there would at a minimum be a tremendous drag on our economic recovery.

It is true that an improving U.S. economy is going to help other nations, both through our lower interest rates and through an expanding U.S. market for their exports -- providing of course that we don't cut them off from that market. But they also have an immediate, short-run financing crunch to get through, and if we don't handle that right there are substantial downside risks for the United States.

This might also be the right context in which to discuss how U.S. participation in the increase in IMF resources would affect the Federal budget and the Treasury's borrowing requirements. Because the United States receives a liquid, interest-earning reserve claim on the IMF in connection with our actual transfers of cash to the IMF, such transfers do not result in net budget outlays or an increase in the Federal budget deficit.

Actual cash transactions with the IMF, under our quota subscription or U.S. credit lines, do affect Treasury borrowing requirements as they occur. An analysis appended to this statement at Annex C presents data on the impact of U.S. transactions between 1970 and 1982 on Treasury borrowing requirements. Although there have been both increases and decreases in Treasury borrowing requirements from year to year, on average there have been increases amounting to $454 million annually over the entire 13 year period, for a cumulative total of over $6 billion. The rate has picked up in the last two years of heavy IMF activity, as would be expected; but the total is still relatively small -- the $454 million annual impact is only a small part of the $54 billion annual average Federal borrowing requirement over the same period, and the $6 billion cumulative impact compares with an outstanding Federal debt of $1.2 trillion at the end of 1982. These figures also serve to demonstrate the revolving nature of the IMF.

° Is the IMF a Bank "Bail-Out"?

I also know there is a widespread concern that an increase in IMF resources will amount to a bank bail-out at the expense of the American taxpayer. Many would contend that the whole debt and liquidity problem is the fault of the banks -- that they've dug themselves and the rest of us into this hole though greed and incompetence, and now we intend to have the IMF take the consequences off their hands. This line of argument is dangerously misleading, and I would like to set the record straight.

First, the steps that are being taken to deal with the financial problem, including the increase in IMF resources, require continued involvement by the banks. Far from allowing them to cut and run, orderly adjustment requires increased bank lending to troubled LDCs that are prepared to adopt serious economic programs. That is exactly what is happening.

And it is not a departure from past experience. I have had Treasury staff review IMF program experience in the 20 countries which received the largest net IMF disbursements in the last few years, to see whether banks had been "bailed out" in the past. Looking at the period from 1977 to mid-1982, they found that for the countries which rely most heavily on private bank financing, IMF programs have been followed up by new bank lending much greater than the amount disbursed by the Fund itself. This also holds true for the 20 countries as a group: net IMF disbursements to this group during the period were $11.5 billion, while net bank lending totalled $49.7 billion, resulting in a ratio of 4.3 to 1 during this period.

Another point I would like to make is that the whole debt and liquidity problem cannot fairly be said to be the fault of the commercial banks. In fact, the banking system as a whole performed admirably over the last decade, in a period when there were widespread fears that the international monetary system would fall apart for lack of financing in the aftermath of the oil shocks. The banks managed almost the entire job of "recycling" the OPEC surplus and getting oil importers through that difficult period. Some of the innovations and decisions that banks made in the process, which seemed rational and necessary at the time to them and to others, may seem doubtful in retrospect, given the way the world economic environment changed. But I think we can agree that governments have had a great deal more to do with shaping that environment than banks.

All of this is not to say that there aren't lessons to be learned in the banking area -- there clearly has been an element of lack of prudence in lending decisions, and of overlending. So we should be asking ourselves: What is there that banks could be doing to improve their screening of foreign loans? What is there that bank regulators could do to improve on their analysis of country risk, examination of bank exposure, and consultations with senior management?

Our basic starting point in addressing these questions is a belief that the U.S. government should not get into the business of dictating the lending practices of private banks. Doing so would inject a political element into what should be business decisions, and would potentially expose the government to liability for covering loans that were not repaid on time. Moreover, in general it is bank managements, which have direct experience and a responsibility to their shareholders and depositors to motivate them, that are in the best position to make lending decisions.

In 1979, the bank regulatory agencies (the Federal Reserve, Comptroller of the Currency and the FDIC) instituted a new system for evaluating country risk, which has four elements. The first is a statistical reporting system designed to identify country exposures at each bank, and to enable regulators to monitor those exposures. Second is an evaluation of each bank's internal system for managing country risk, aimed at encouraging more systematic review of prospective loans. Third, where there is a judgment by regulators that a country has interrupted its debt service payments, or is about to do so, all loans to that country may be "classified" as substandard, doubtful, or a total loss, and such "classification" may trigger an obligation by the bank to set aside precautionary loan loss reserves. Fourth, bank examiners review and comment upon each bank's large foreign lending exposures, drawing upon the findings of an interagency committee of country analysts.

There are several possible changes that could be made in the regulatory environment. One would be to set up formal limits on each bank's exposure in different countries by law or regulation, in effect setting up "single country" limits analogous to the "single borrower" limits which are already used. Such limits on country exposure could be highly arbitrary and unable to distinguish among the capabilities of different banks or among the size and financial health of different countries -- particularly if dictated specifically, once and for all, in legislation. If limits were applied judgmentally, on the other hand, they could require that the U.S. government make controversial economic and political judgments about other countries. It may be feasible and desirable to do something more along these lines, but we should not put ourselves in too tight a corner on either count, and thus should try to leave as much scope as possible for bank regulators to work out the details.

Another possibility, which has been discussed with banks here and abroad, would be to require banks to meet specific criteria in establishing precautionary loan loss reserves against troubled loans, or against particularly large ones. Current procedures are not uniform across banks, and since setting aside such reserves reduces current earnings, there is some reluctance to do so unless absolutely required.

Both in the banking regulatory agencies, and at the Treasury, we will be reviewing these and other issues to see what changes might be desirable. We need to be careful in determining how to deal with such a sensitive and central part of our economy. Any decisions in this area will have important implications both for resolving the present situation, and for the evolution of the banking system in the future.

The Multilateral Development Banks

I would like to close with some remarks about our proposals for U.S. participation in the multilateral development banks (MDBs). This year, the Administration will be seeking Congressional approval of legislation to authorize U.S. participation in replenishments of the Inter-American Development Bank, the Asian Development Bank, and the African Development Fund.

The MDBs are proven, effective instruments for promoting economic growth and development, and our participation in the MDBs represents a significant part of both present and projected U.S. foreign assistance. We have been making a major effort to further improve the effectiveness of these institutions so as to maximize the contribution they make to sustainable economic development.

The objectives of MDB programs are markedly different from those of the IMF. The IMF provides temporary financing designed to support orderly adjustment and to safeguard the functioning of the international monetary system. Its resources are available for drawing by all members. In contrast, the MDBs lend primarily to finance portions of specific investment projects. MDB financing is longer term -- 20 years or more -- and it is available only to developing countries.

Given the leadership role of the United States in the international community and the great diversity of U.S. interests, we must be able to deliver on the internationally negotiated funding arrangements for the MDBs. To this end, the Administration has consulted closely with the Congress both before and during the MDB funding negotiations.

When these have been completed, we will be proposing legislation to authorize appropriations of $960 million for the concessional lending programs of the Inter-American and Asian Development Banks and the African Development Fund. This respresents a 24.5 percent reduction from the previous replenishments for these programs. At the same time, other donors will be providing more than $4 billion.

Agreements are nearing completion for the replenishment of resources of the Inter-American and Asian Development Banks. When these are completed, we will be proposing legislation to authorize an increase in U.S. participation in the African Development Fund and the capital and concessional lending programs of the Inter-American and Asian Development Banks. These are larger in total than the previous replenishments -- but U.S. subscriptions will require less budget authority, since the development banks will rely more heavily on the private market and there will be an overall reduction in the concessional windows.

The African Development Fund (AFDF)

Draft legislation authorizing a U.S. contribution to the third replenishment of the African Development Fund was submitted to the 97th Congress but was not enacted. U.S. participation in this replenishment is not only an important way of demonstrating our continued commitment to economic growth and development in the world's least developed continent, but also reflects increased U.S. economic, political, and security interests in that region.

As a result of provisions contained in the replenishment agreement, the Fund currently has a backlog of approved loans that cannot be signed until the United States agrees to participate in the replenishment and makes its first payment. The replenishment, which is to finance lending in the 1982-84 period, totals about $1.1 billion. The proposed U.S. share is $150 million, or 14 percent of the total. Appropriations for the first $50 million installment would be provided under the FY 1983 Continuing Resolution and the two remaining installments will be sought in fiscal years 1984 and 1985.

Inter-American Development Bank (IDB) Sixth Replenishment

While negotiations for the Sixth Replenishment of the Inter-American Development Bank have not been concluded, we expect the final agreement to entail U.S. budgetary outlays at a lower level than the previous replenishment. Our present expectation is that this replenishment will provide a $13 billion lending program funded over a four-year period beginning in fiscal 1984, and will call for a capital increase of $14.8 billion, with a paid-in component of 4.5 percent. We also expect agreement to a replenishment of the Fund for Special Operations (FSO) totalling $725 million. The overall replenishment would result in U.S. capital subscriptions of $5,156 million, with paid-in capital of $232 million ($58 million annually) and callable capital of $4,924 million ($1,231 million annually), and in U.S. contributions to the FSO of $290 million ($72.5 million annually).

This proposed replenishment is consistent with the recommendations of the Administration's MDB Assessment for reduction of soft window contributions and paid-in capital, while still providing assistance to the poorest developing countries. The FSO would be about $1 billion less than that of the last replenishment, with total budgetary saving to the United States as compared to the previous replenishment of $384 million. This will be the first IDB replenishment where all borrowing member countries provide all of their paid-in capital subscriptions and FSO contributions in convertible currency, a solid example of the willingness of the more advanced developing countries to assume greater responsibility in the international economic system.

In order to obtain support for the scaled-back FSO replenishment, the United States agreed to the establishment of an Intermediate Financing Facility (IFF) to be targeted at the region's poorer countries. Funding for the IFF would come from FSO net income and FSO general reserves, and would be combined with regular hard loans. The IFF would be used to lower the interest cost on IDB hard window loans by approximately 5 percentage points and, as presently envisioned, would not require any new contributions.

Inter-American Investment Corporation (IIC)

Partially modeled after the International Finance Corporation, the Inter-American Investment Corporation would be a separate entity which provides development assistance to the private sector in Latin America and the Caribbean. The member countries of the Inter-American Development Bank have discussed formation of such a Corporation for a number of years and a meeting will be held this month to finalize an agreement on the capitalization of the IIC. Assuming there is adequate support from other IDB member countries, we currently envision U.S. subscriptions of up to $20 million annually over four years, beginning in FY 1984.

The Asian Development Bank (Third GCI)

We expect negotiations to conclude soon on the third general capital increase to finance ADB's ordinary capital lending for the CY 1983-1987 period. ADB management has moved from an initial proposal for a 125 percent GCI with 10 percent paid-in to a proposal for a 105 percent GCI with 5 percent paid-in. We expect to join a consensus of ADB member countries on this proposal in the near future.

In terms of U.S. budgetary costs, the current proposal represents a U.S. paid-in capital subscription of $66.2 million ($13.2 million annually) and a U.S. callable capital subscription of $1,257 million ($251.4 million annually) over five years.

Asian Development Fund

During 1982, the Administration completed negotiations on the fourth replenishment of the Asian Development Fund and now seeks authorization of U.S. participation in the replenishment.

The U.S. $520 million share of the proposed replenishment is 16.25 percent of the total as compared to a 22 percent U.S. share in the previous replenishment. Appropriations of $130 million annually will be sought in the four year period from FY 1983 through 1986.

Conclusion

The IMF plays a crucial role in the solution to current debt and liquidity problems, and in providing the environment for world recovery. It is absolutely essential that the proposed increase in IMF resources become effective by the end of this year, to enable the IMF to meet these responsibilities. Prompt U.S. approval is important not only because the financing is needed, but also because it would be a sign of confidence to other governments and to the public, and would help lay to rest concerns about the risks to global recovery.

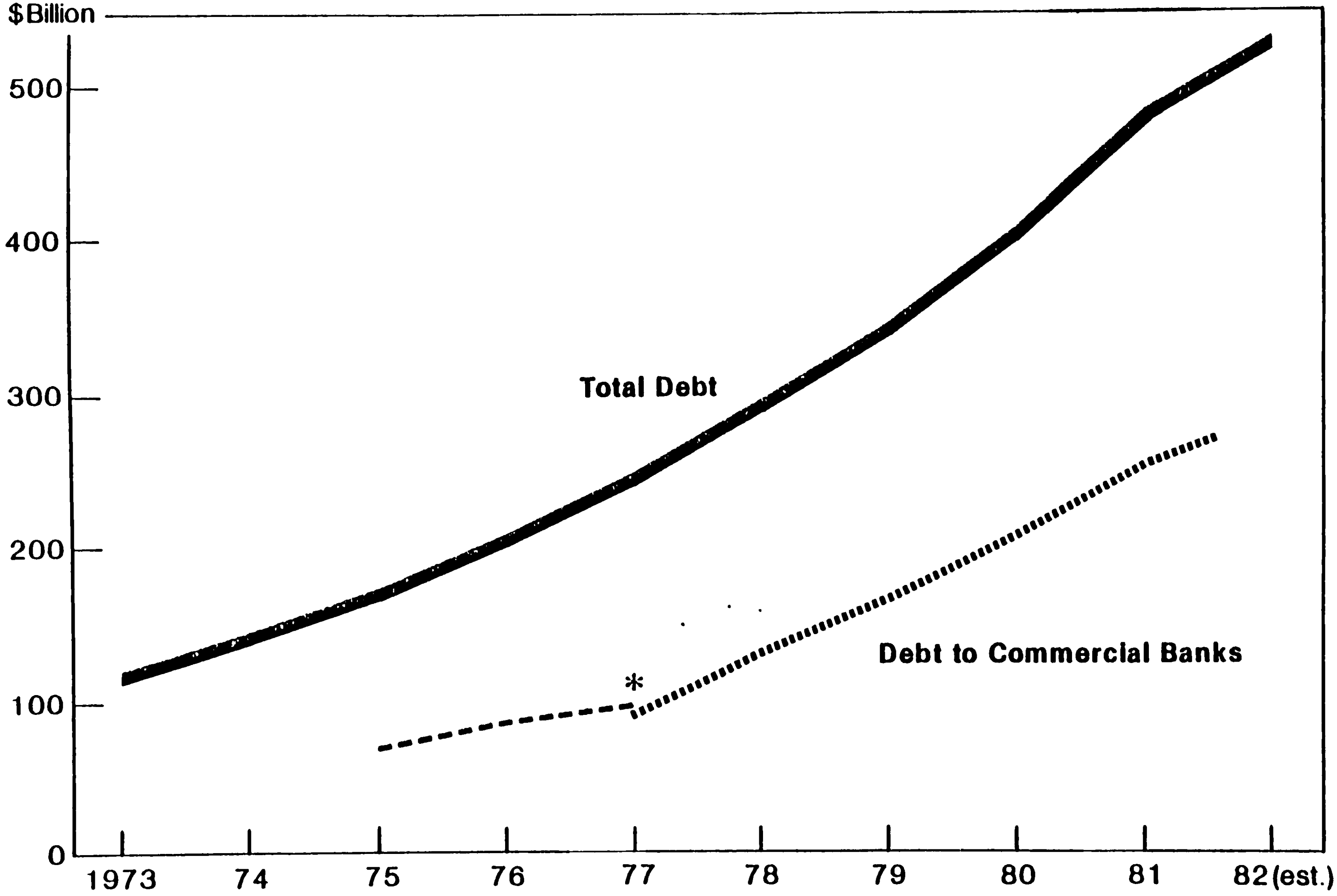
But most importantly, timely approval of these proposals is essential to our own economic interests -- to the prospects for American businesses and American jobs. The legislation will be submitted to you in a very few days. I urge that you give it prompt and favorable consideration.

Both the IMF and the multilateral development banks also serve broader U.S. political and security interests. To the rest of the world they are a sign that the bulwark of democracy is also a responsible partner in international economic affairs. To the poorer nations of the world the multilateral development banks are also tangible evidence of the support by Western nations for sustainable economic development. And of direct benefit to the United States, they help to foster political stability and democratic values in the developing world.

I have tried to lay out a number of reasons for the United States to support the IMF and the MDBs. Some of these are at least partly altruistic, but the majority relate to our own self-interest. I urge your strong support for the proposed U.S. appropriations for these institutions.

Chart A

OUTSTANDING FOREIGN DEBT OF NON-OPEC LDCs

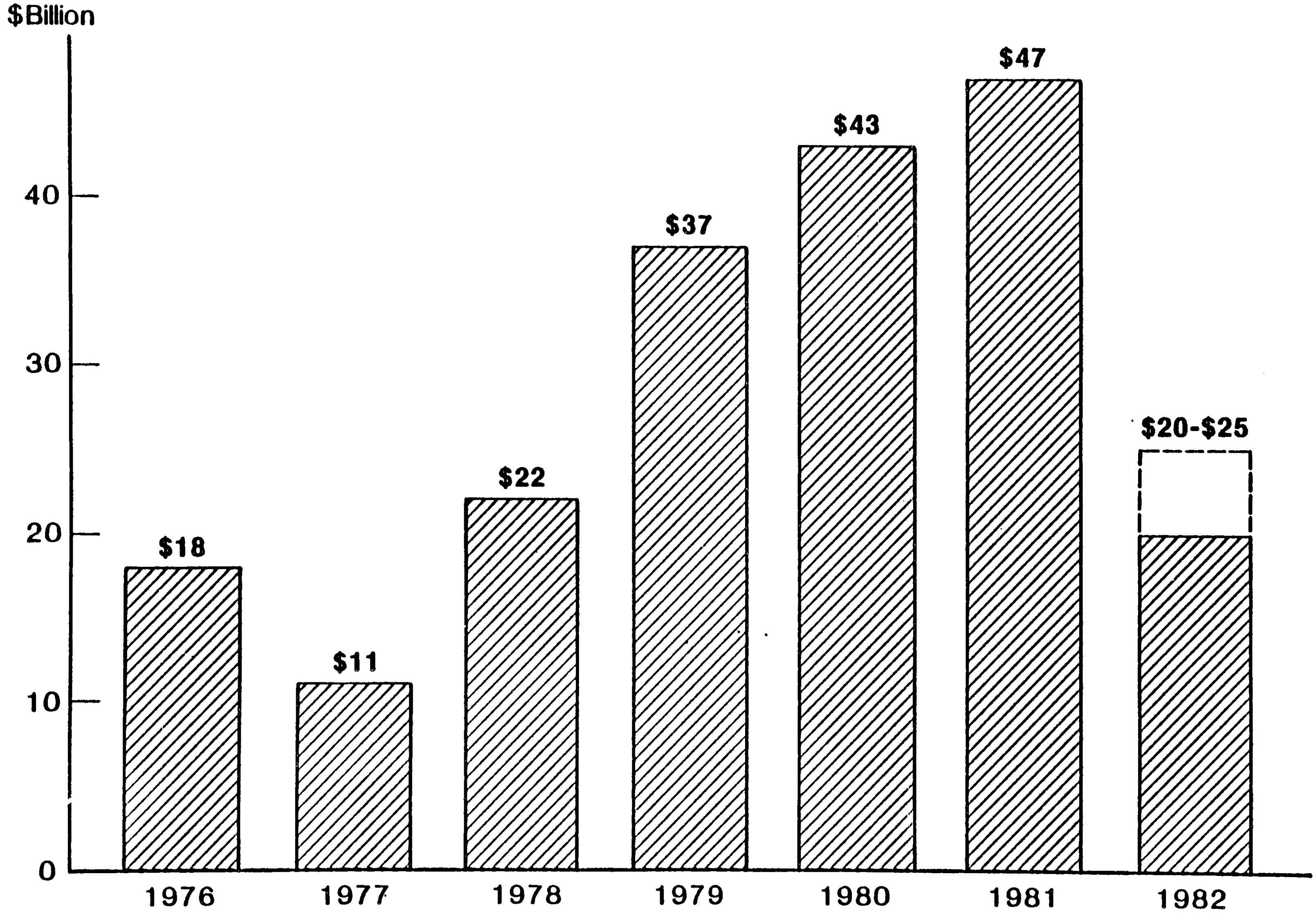


* Series break.

U.S. Treasury Dept.
2-11-83

Chart B

NET NEW LENDING BY COMMERCIAL BANKS TO NON-OPEC LDCs



U.S. Treasury Dept.
2-11-83

Chart C

GROWTH OF U.S. AND WORLD EXPORT VOLUME

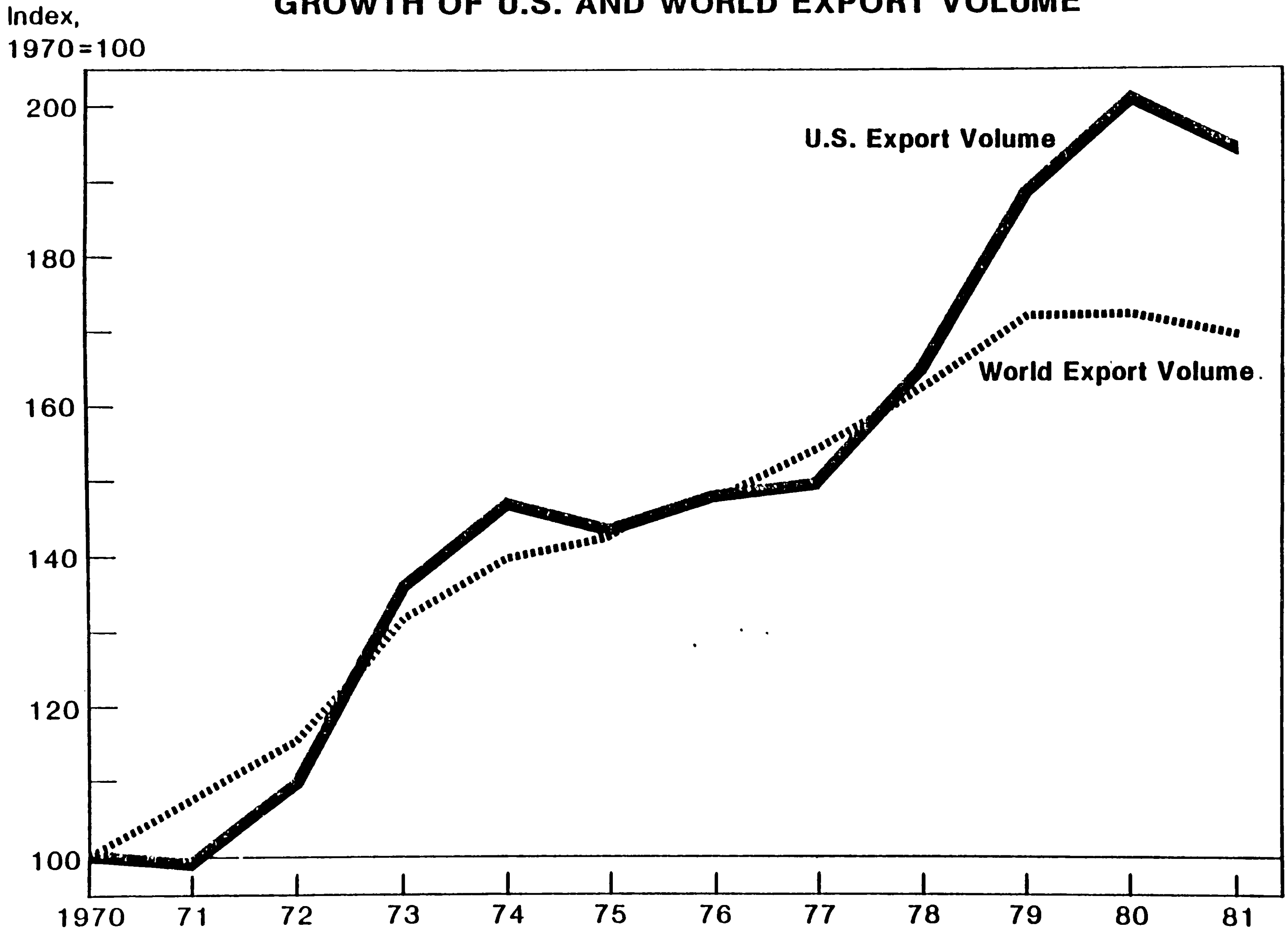
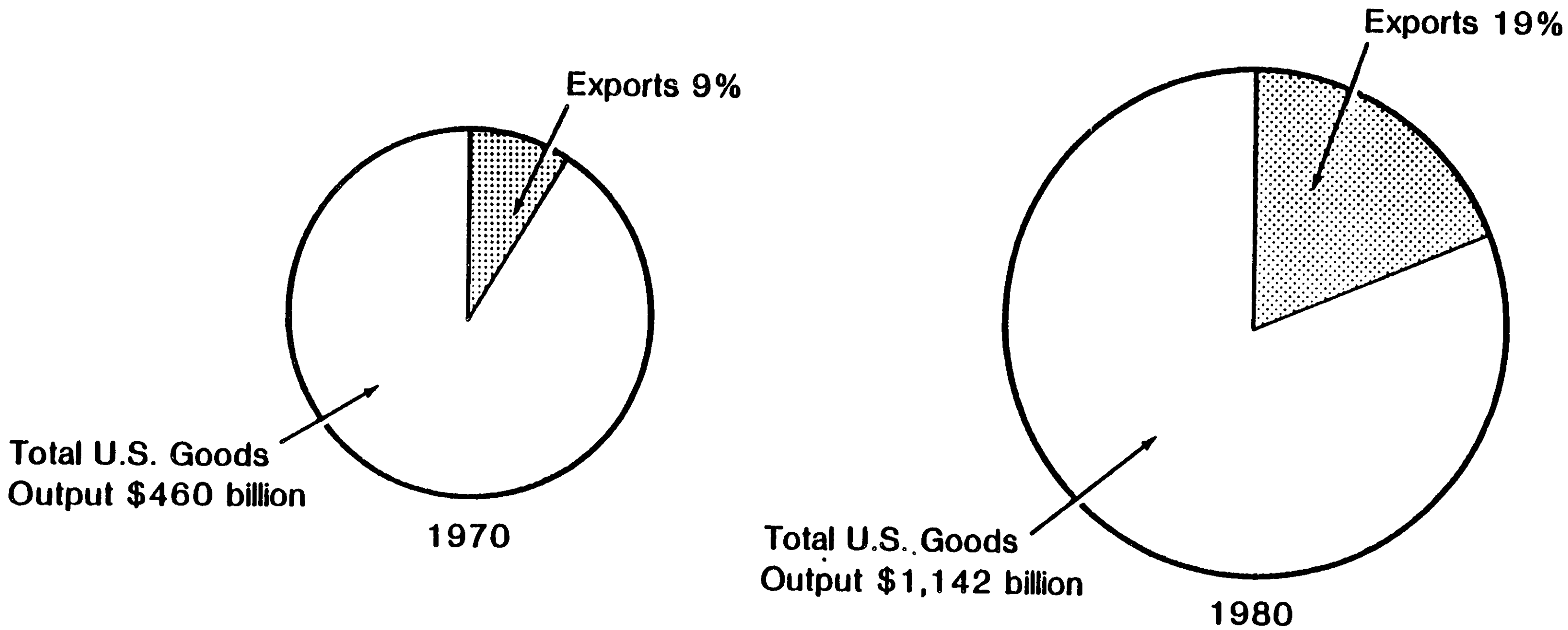


Chart D

SHARE OF U.S. EXPORTS IN TOTAL U.S. GOODS OUTPUT

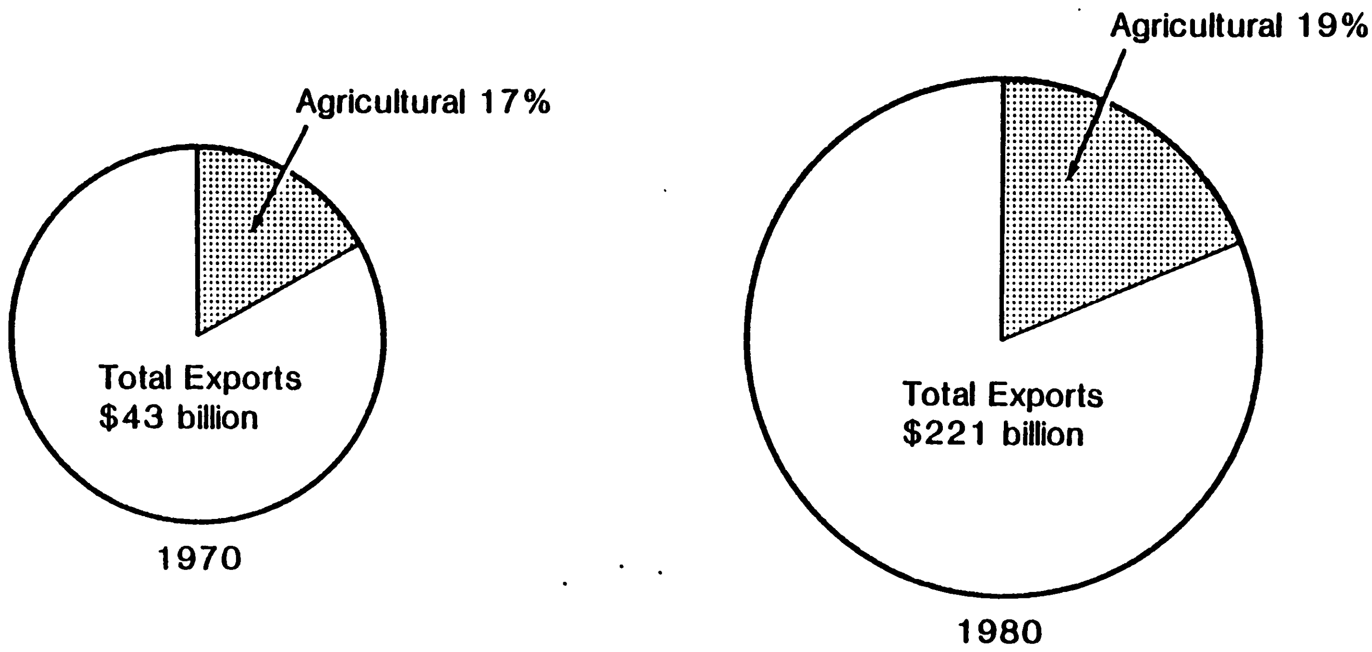


U.S. Treasury Dept.
2-11-83

Chart E

U.S. AGRICULTURAL EXPORTS

Share in Total U.S. Exports:



Net U.S. Agricultural Trade Balance:

Surplus of $1.6 billion

Surplus of $24.3 billion

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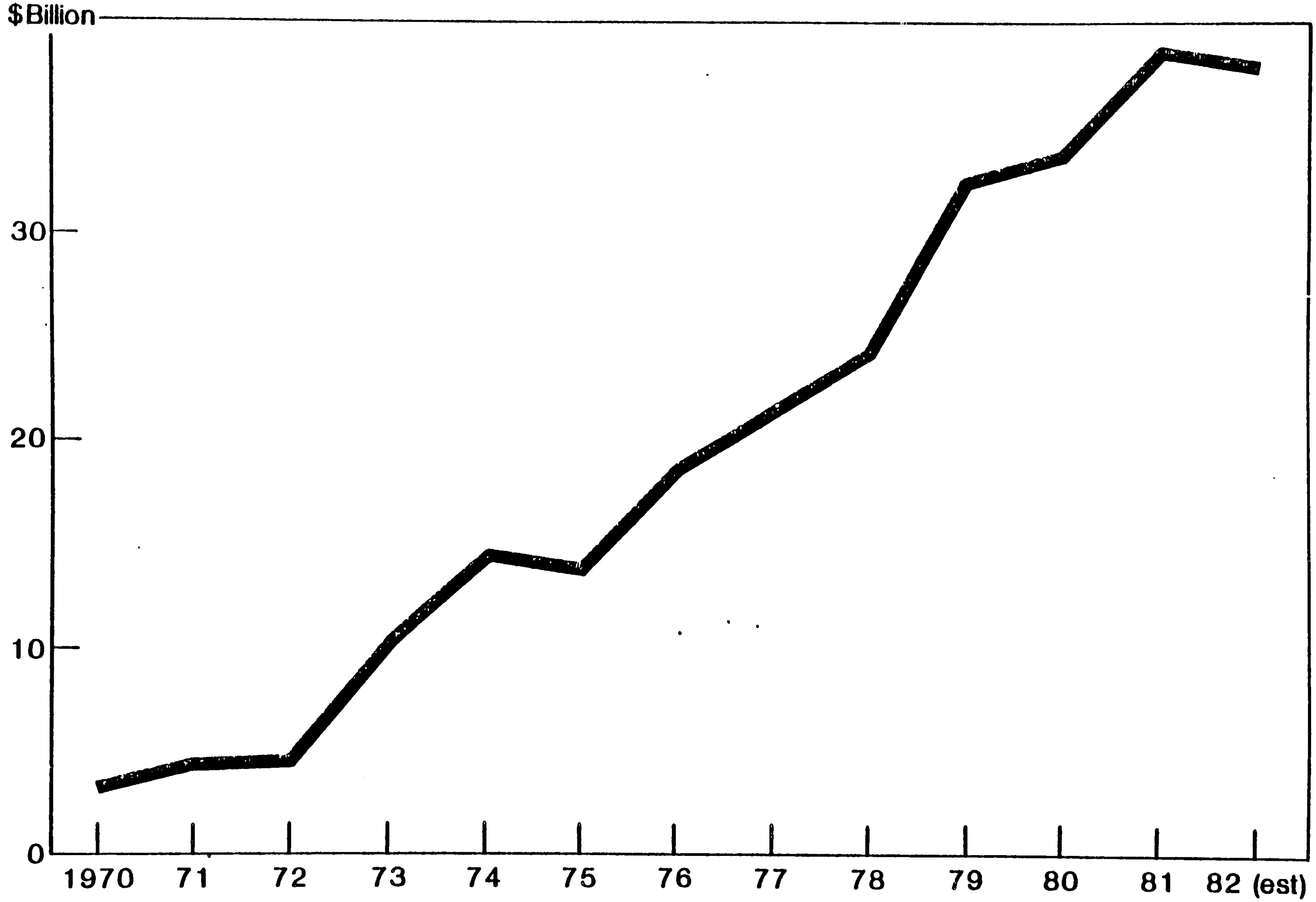
2-11-83

Chart F

U.S. TRADE BALANCE IN SERVICES



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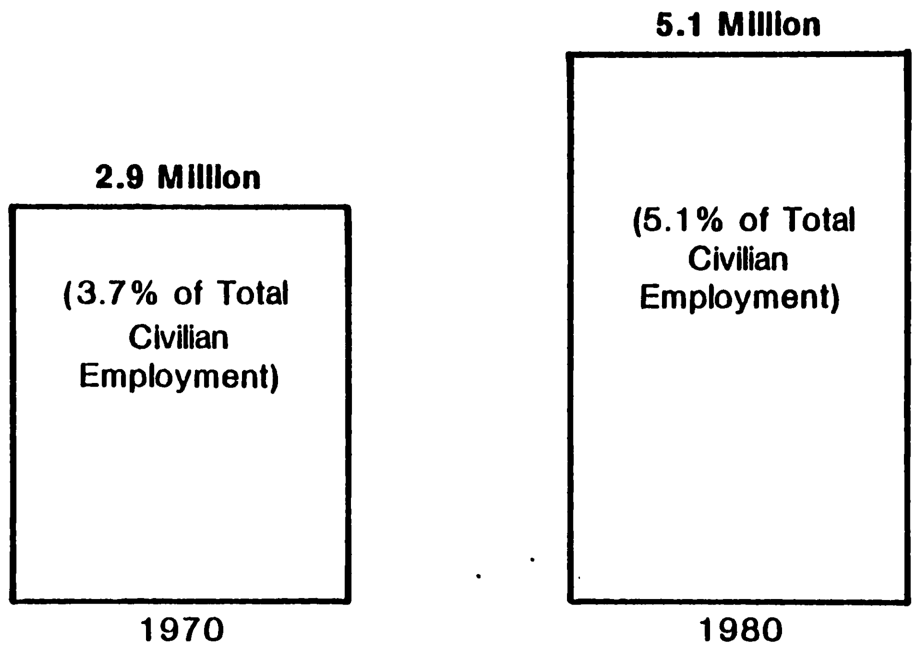
2-11-83

Chart G

U.S. EXPORT-RELATED JOBS



As of 1980, each $1 billion of U.S. exports was estimated to result in 24,000 jobs.

Source: Commerce Department (ITA) estimates.

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2-11-83

Chart H

U.S. EXPORTS TO NON-OPEC LESS DEVELOPED COUNTRIES

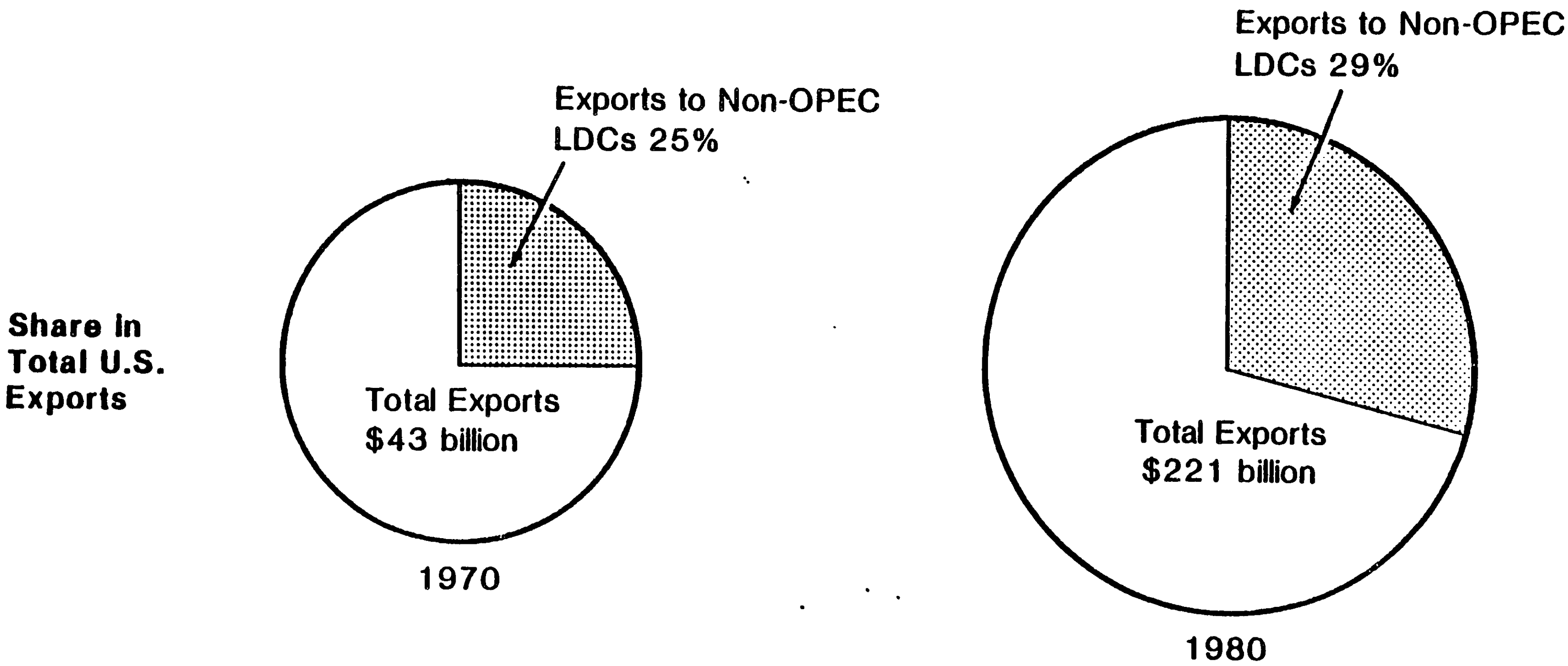

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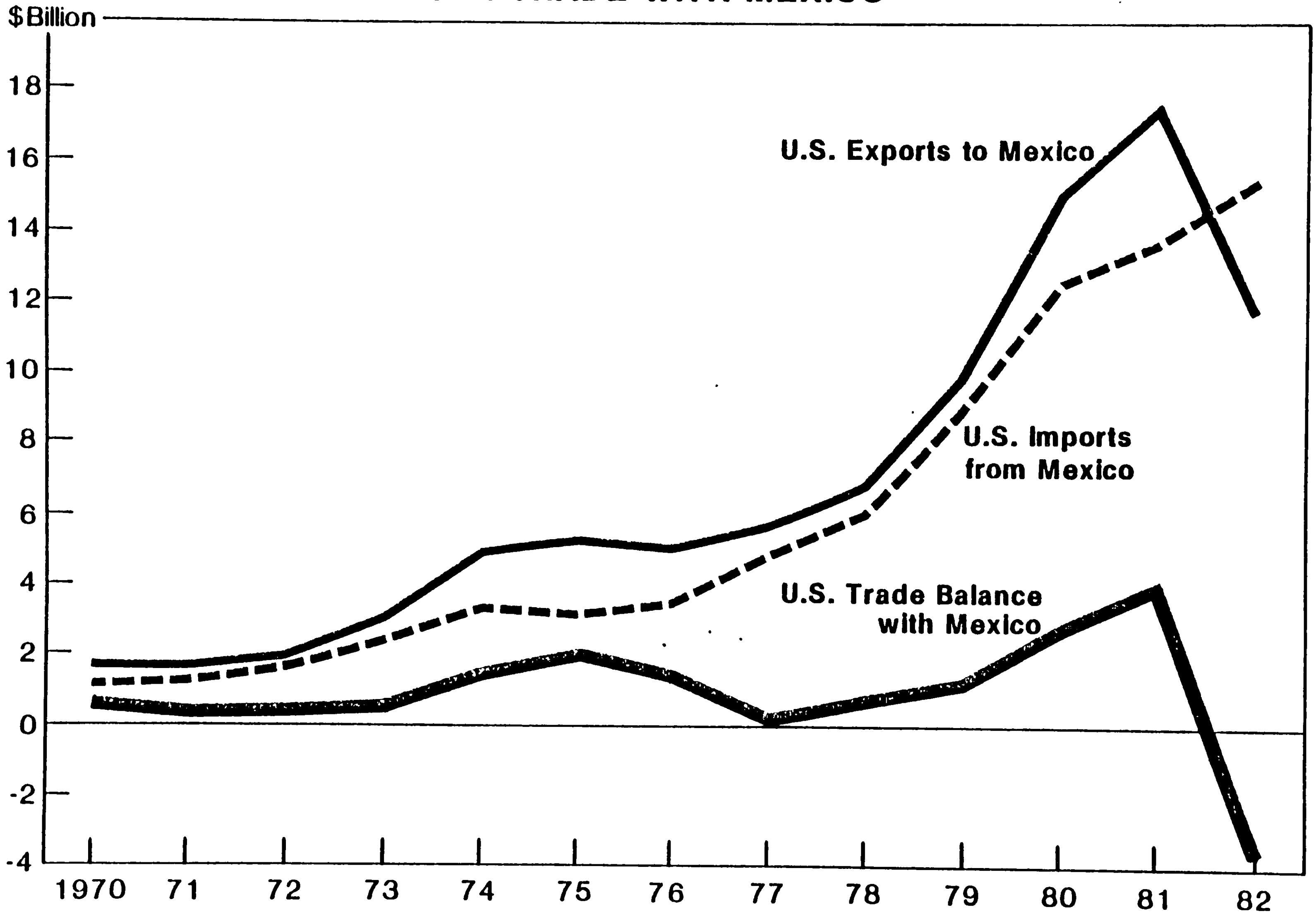
Chart I

U.S. TRADE WITH MEXICO



U.S. Treasury Dept.
2-11-83

APPENDIX A

INTERNATIONAL MONETARY FUND

Press Release NO. 83/11

FOR IMMEDIATE RELEASE
February 11, 1983

Press Communiqué of the Interim Committee
of the Board of Governors of the
International Monetary Fund.

1. The Interim Committee of the Board of Governors of the International Monetary Fund held its twentieth meeting in Washington, D.C., on February 10 and 11, 1983, under the chairmanship of Sir Geoffrey Howe, Chancellor of the Exchequer of the United Kingdom. Mr. Jacques de Larosière, Managing Director of the International Monetary Fund, participated in the meeting. The meeting was also attended by observers from a number of international and regional organizations and from Switzerland.

2. The Committee discussed the World Economic Outlook and the policies needed to cope with the difficult problems faced by most members of the Fund.

The Committee noted that estimated rates of both growth of output and inflation had been revised downward since its previous meeting in September 1982. Anxiety was expressed at the high level of unemployment and the weakness of investment and world trade, against the background of only limited indications of economic recovery. At the same time, the Committee welcomed the further progress made by some of the larger industrial countries in their fight against inflation, as well as the reduction in interest rates that had been facilitated by this progress--developments that were providing the basis for a sustainable recovery in economic activity.

Believing that successful handling of the inflation problem is a necessary--albeit not sufficient--condition for sustained growth over the medium term, the Committee urged national authorities, in their efforts to promote sustained recovery, to avoid measures that might generate harmful expectations with regard to inflation. The importance of reducing fiscal deficits in a number of countries was also emphasized. Otherwise, the Committee noted, high real interest rates detrimental to the process of recovery could be generated by market expectations regarding government borrowing requirements.

It was the Committee's view that, in several major industrial countries where inflation remained relatively high, present circumstances called for continued restraint in monetary and fiscal policies, along with effective implementation of the incomes policies now in place. It was felt, however, that conditions for economic recovery had improved in those large industrial countries that have been able

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to achieve the greatest measure of success in reducing and controlling inflation. This success--and the reduction in interest rates that it has permitted--provided the basis, within the pursuit of counter-inflationary monetary and fiscal policies, for greater real growth of activity. The transition to a more stable path of real growth would be further facilitated by determined efforts to reduce market rigidities and structural imbalances.

The Committee deplored the upsurge of protectionist pressures in the past year or two. It stressed the paramount importance of resisting these pressures and, indeed, rolling them back.

The unsatisfactory situation facing non-oil developing countries was a source of particular concern to the Committee, which noted that growth rates in these countries, after averaging about 6 per cent in the 1960s and early 1970s, had averaged only 2 1/2 per cent during the past two years and were not expected to show much improvement in 1983. The Committee also observed that the modest recent increases in output, which were barely sufficient to keep pace with rapid population growth, had been achieved against a background of deteriorating terms of trade, sluggish markets for exports, high interest rates in international financial markets, and strains in the financing of current account deficits. These conditions had necessitated a sharp compression of imports by the non-oil developing countries--which, in turn, had been achieved at the cost of lower investment and growth.

Noting the extent of the external adjustment already achieved by many non-oil developing countries and the uncertainties that most such countries face in financing their current account deficits, the Committee attached great importance to the continuing provision of both official development assistance and private banking flows on an adequate scale, and it welcomed the special role recently played by the Fund in this connection.

More generally, the Committee stressed the enhanced importance, in current circumstances, of the Fund's role in providing its balance of payments assistance to member countries that engage in adjustment programs and in exercising firm surveillance over policies, and also the need to equip the Fund with adequate resources to perform this role.

3. The Committee, noting the progress made by the Executive Board on the various issues of the Eighth General Review of Quotas, focused its attention on the remaining issues, and took satisfaction in being able to reach the following agreement on the subject of quotas:

(a) The total of Fund quotas should be increased under the Eighth General Review from approximately SDR 61.03 billion to SDR 90 billion (equivalent to about US$ 98.5 billion).

(b) Forty per cent of the overall increase should be distributed to all members in proportion to their present individual quotas, and the balance of sixty per cent should be distributed in the form of selective adjustments in proportion to each member's share in the total of the calculated quotas, i.e., the quotas that broadly reflect members' relative positions in the world economy.

(c) Twenty-five per cent of the increase in each member's quota should be paid in SDRs or in usable currencies of other members.

The Committee considered the possibility of a special adjustment of very small quotas, i.e., those quotas that are currently less than SDR 10 million. It was agreed to refer this matter to the Executive Board for urgent consideration in connection with the implementation of the main decision.

4. The question of the limits on access to the Fund's resources was raised in the Committee. It was noted that the Executive Board will review this matter before June 30, 1983. The Committee invited the Executive Board to take note of the views expressed in the Committee by those favoring maintenance of the present enlarged limits in terms of multiples of quotas and also by those stressing the need to have regard to developments in the Fund's liquidity. It also invited the Managing Director to report on this matter at the next meeting of the Committee.

5. The Committee noted the recent decision of the Finance Ministers and Central Bank Governors of the participants in the General Arrangements to Borrow (GAB) to support an increase in the total amount of the commitments under these Arrangements to SDR 17 billion (equivalent to about US$19 billion) and to make the resources of these Arrangements available to the Fund to finance also purchases by nonparticipants when the Fund faces an inadequacy of resources arising from an exceptional situation involving a threat to the stability of the international monetary system. In this connection, the Committee welcomed the intention of Switzerland to become a full participant in the Arrangements, through the Swiss National Bank, with a credit commitment of SDR 1,020 million.

The Committee also welcomed the willingness of Saudi Arabia to provide resources to the Fund, in association with the GAB, and for the same purposes as those of the GAB. They noted with satisfaction the progress that is being made in setting out the detailed features of this association.

6. The members of the Committee requested the Executive Board to adopt, before the end of February 1983, the necessary decisions and other actions to implement the consensus reached in the Committee. They also agreed to urge the governments of their constituencies to act promptly so that the proposals for the increase in the Fund's resources could be made effective by the end of 1983.

7. The Committee considered again the question of allocations of SDRs in the current, i.e., the fourth, basic period which began on January 1, 1982. Noting the developments since its Toronto meeting, the Committee agreed that the matter should be reexamined as soon as possible. It, therefore, requested the Executive Board to review the latest trends in growth, inflation and international liquidity, with a view to enabling the Managing Director to determine, not later than the next meeting of the Interim Committee, whether a proposal for a new SDR allocation could be made that would command broad support among members of the Fund.

8. The Committee agreed to hold its next meeting in Washington, D.C., on September 25, 1983.

January 19, 1983

Press Communique of the Ministers and Governors of The Group of Ten

1. The Ministers and central bank Governors of the ten countries participating in the General Arrangements to Borrow (GAB) met in Paris on January 18, 1983 under the chairmanship of Mr. Jacques Delors, Minister of Economy and Finance of France. The Managing Director of the International Monetary Fund (IMF), Mr. Jacques de Larosière, took part in the meeting, which was also attended by Mr. F. Leutwiler, President of the Swiss National Bank, Mr. E. Van Lennep, Secretary-General of the Organisation for Economic Cooperation and Development (OECD), Mr. A. Lamfalussy, Assistant General Manager of the Bank for International Settlements, and Mr. F.-X. Ortoli, Vice-President of the Commission of the European Communities.

2. The Ministers and Governors heard a report by the Chairman of their Deputies, Mr. Lamberto Dini, on issues relating to the revision and expansion of the GAB and the Eighth General Review of Quotas of the IMF. They also heard a report by the Chairman of the Working Party No. 3 of the Economic Policy Committee of the OECD, Mr. Christopher Mcmahon, on the world economic outlook.

3. In addressing the world economic situation, the Ministers and Governors welcomed recent successes in the fight against inflation and prospects for further progress. They looked toward sound monetary and fiscal policies and appropriate moderation in the growth in incomes to encourage lower interest rates, expanding trade, higher employment, and durable economic growth. These desirable developments must not be thwarted by trade restrictions or by disruption of the international financial system. At the same time, it was recognized that soundly based growth would itself help ease current tensions. To these ends, the Ministers and Governors affirmed their support for a reinforced cooperation among industrialized countries on economic, financial, and trade policies. They considered that a sustainable improvement in activity in the industrial countries in 1983 can make an important contribution to a lasting solution of the indebtedness problem of many developing countries and to limiting the unemployment problem in all countries. Therefore, they noted with satisfaction that the competent international organizations will examine whether further steps can be taken to ensure renewed and sustained growth, and will report to the next ministerial councils, notably in the OECD and IMF framework.

4. Against this background, the Ministers and Governors discussed the international financial situation. They noted that, while strains remained in the system and the foreign debt problems of a number of countries were still a cause for real concern, governments and monetary authorities had been cooperating actively and effectively with international monetary institutions and commercial banks to reinforce the stability of the system. In order to ensure the continuing ability of the financial system to cope with existing strains and to facilitate the adjustment process, they strongly supported a substantial increase of resources available to the International Monetary Fund.

5. In light of the foregoing, the Ministers and Governors have decided, subject to the necessary legislative approval, that their aggregate credit commitments under the GAB should be promptly increased—from SDR 6.4 billion to SDR 17 billion (equivalent to an increase from $7.1 billion to about $19 billion). They welcomed the intention of Switzerland to become a full-scale participant in the GAB and decided that necessary adjustments in the arrangements should be made so as to permit the participation of Switzerland at an early date. They also decided an adjustment of the participants' shares in the arrangements so as to reflect better their size and role in the international economy and their ability to provide financial resources. A list of the new credit commitments that have been agreed is attached. They further agreed that in the future the GAB would be available not only for drawings by participants but also for purchases from the Fund for conditional financing for all its members, including members that are not GAB participants, when the Fund was faced with an inadequacy of resources arising from an exceptional situation associated with requests from countries with balance of payments problems of a character or of aggregate size that could pose a threat to the stability of the international monetary system.

6. The Ministers and Governors also looked to the conclusion of arrangements with other countries that might be willing and able to provide substantial resources to the Fund for the same purposes and on terms not unlike those agreed under the GAB. In this regard, the Ministers and Governors welcomed the recent contacts that the Chairman of the Group of Ten, and the

Chairman of the Interim Committee and the Managing Director of the Fund, have had with the authorities of Saudi Arabia. They asked the Chairman of the G-10 Deputies, in collaboration with the Managing Director of the IMF, to resume such contacts as soon as possible.

7. The Ministers and Governors discussed the issues related to the Eighth General Review of Quotas. They agreed that a substantial overall increase was called for. They also recognized the need for a meaningful adjustment of quota shares in the Fund to bring these more in line with the relative position of member countries in the world economy.

8. The Ministers and Governors noted that substantial progress had been made on the Quota Review issues, and were of the view that the conditions were now present for reaching conclusions at the forthcoming meeting of the Interim Committee on February 10-11, 1983. They emphasized the desirability of having new quotas in effect by the end of 1983.

9. The Ministers and Governors expressed their gratitude to the French authorities for their cordial hospitality and for the excellent meeting arrangements.

Attachment

ATTACHMENT

GAB Credit Commitments for G-10 Countries and Switzerland

	In millions of SDRs	Shares in per cent
United States	4,250.0	25.00
Germany	2,380.0	14.00
Japan	2,125.0	12.50
France	1,700.0	10.00
United Kingdom	1,700.0	10.00
Italy	1,105.0	6.50
Canada	892.5	5.25
Netherlands	850.0	5.00
Belgium	595.0	3.50
Sweden	382.5	2.25
Switzerland	1,020.0	6.00
Total	17,000.0	100.00

APPENDIX B

IMF Drawings by the United States

The United States has drawn on the International Monetary Fund (IMF) on twenty-four occasions over the past 19 years for a total of about SDR 5.8 billion (equivalent to about $6.5 billion at the exchange rates prevailing at the time of each drawing), the second largest amount of cumulative drawings of any IMF member. None of these drawings was subject to IMF policy conditionality, as they all involved drawings on the U.S. reserve position in the IMF. Drawings on the reserve position are available automatically upon representation of balance of payments need; do not bear interest and are not subject to repurchase obligations; and do not involve policy conditionality.

The U.S. drawings were for the following purposes: during the 1960s and early 1970s they were designed to limit foreign purchases of U.S. gold reserves; subsequently, they were designed to provide the United States with foreign currencies for the purpose of exchange market operations. These purposes are explained below. A table listing all U.S. drawings is attached.

Drawings During the 1960s and 1970s

Under the international monetary arrangements in operation following World War II, each member of the IMF was required to establish and maintain a "par value" for its currency in terms of gold. The United States undertook to fulfill its par value obligations by standing ready to convert dollars held by foreign monetary authorities into gold at the official price of $35 per ounce -- i.e., the par value of the dollar. Other countries met their par value obligations by maintaining exchange rates for their currencies -- directly or indirectly -- in terms of the dollar within narrow margins. In this manner, a strucuture of currency exchange rates linked to gold was established and maintained.

During the 1950s and 1960s, large payments imbalances, substantial losses of U.S. gold and foreign accumulations of dollar holdings, representing further potential strains on U.S. gold, put increasing strain on this system. Beginning in the early 1960s the United States, in cooperation with foreign monetary authorities, initiated a variety of measures designed to limit pressures on U.S. gold holdings. U.S. drawings on the IMF were an integral part of this program.

In general, IMF drawings provided the United States with foreign currencies that could be used to purchase dollars from foreign monetary authorities and thus reduce demands for conversion of official dollar holdings to gold. The foreign currencies obtained from the IMF were used most often in the following types of transactions:

-- to facilitate repayment of IMF drawings by other countries without necessitating the use of U.S. gold;

-- repayment of U.S. short-term currency swaps with foreign central banks; and

-- direct purchases by the United States of foreign official dollar holdings that would otherwise be used to purchase U.S. gold.

Drawings Since the Early 1970s

With the end of the par value/gold convertibility arrangements in the early 1970s, the basic purpose of U.S. drawings from the IMF was to finance U.S. intervention in the exchange markets in support of the dollar. During the 1970s, the U.S. intervened directly in the foreign exchange market, buying and selling foreign currencies for dollars, in order to deal with exchange market pressures on the dollar. The foreign currencies obtained from U.S. drawings in the IMF provided an important source of funds for such intervention. In November 1978, a U.S. drawing of $3 billion of German marks and Japanese yen was a component of a major program of U.S. and foreign intervention in the exchange market to support the dollar.

IMF Drawings by the United States
(SDR Millions)

Date		Amount
1964:	Feb	125
	June	125
	Sept	150
	Dec	125
	Total	525
1965	March	75
	July	300
	Sept	60
	Total	435
1966	Jan	100
	March	60
	April	30
	May	30
	July	71
	Aug	282
	Sept	35
	Oct	31
	Nov	12
	Dec	30
	Total	681

Date		Amount
1968:	March	200
	Total	200
1970:	May	150
	Total	150
1971:	Jan	250
	June	250
	Aug	862
	Total	1,362
1972:	April	200
	Total	200
1978:	Nov	2,275
	Total	2,275
Grand Total		5,828 1/

1/ Equivalent to about $6.5 billion at exchange rates prevailing at the time of each drawing.

Budgetary and Accounting Treatment of Transactions with the IMF under the U.S. Quota in the IMF and U.S. Loans to the IMF

Under budget and accounting procedures established in consultation with the Congress at the time of the 1980 increase in the U.S. IMF quota, an increase in the U.S. quota or line of credit to the IMF requires budget authorization and appropriation for the full amount of increases in the quota or U.S. lending arrangements. The sum is included in the budget authority totals for the fiscal year requested. Payment to the IMF of the increased quota subscription is made partly (25 percent) in reserve assets (SDRs or foreign currencies) and partly in non-interest bearing letters of credit, which are a contingent liability. Under the credit lines established pursuant to IMF borrowing arrangements with the United States, the Treasury is committed to provide funds upon call by the IMF.

A budget expenditure occurs only as cash is actually transferred to the IMF, through the 25 percent reserve asset payment, through encashment of the quota letter of credit, or against the borrowing arrangements. Simultaneous with such transfers, the U.S. receives an equal offsetting receipt, representing an increase in the U.S. reserve position in the IMF -- an interest-bearing, liquid international monetary asset that is available unconditionally to the United States in case of balance of payments need. As a consequence of these offsetting transactions, transfers to the IMF under the quota subscription or U.S. lending arrangements therefore do not result in net budget outlays, or directly affect the budget deficit. Similarly, payments of dollars by the IMF to the United States (for example, resulting from repayments by other IMF member countries) do not result in net budget receipts since the U.S. reserve position declines simultaneously by a like amount.

Transfers from the United States to the IMF under the U.S. quota or U.S. lending arrangements increase Treasury borrowing requirements, while transfers from the IMF to the United States improve the Treasury's cash position and reduce its borrowing requirement. The net effect of transfers to and from the IMF has varied widely over the years, resulting in cash outflows from the Treasury in some years and inflows to the Treasury in other years. Moreover, Treasury interest costs on borrowings to finance any net transfers to the IMF need to be balanced against the remuneration (interest) earned on the U.S. reserve position in the IMF. Finally, the U.S. may incur exchange gains and losses on the U.S. reserve position in the IMF due to changes in the dollar value of the SDR.

It is not possible to project the effect on Treasury borrowing requirements or the net cost of U.S. transactions with the IMF because of uncertainties regarding the future level of IMF financing; the portion of such financing that would be in dollars; and movements in market interest and exchange rates. However, the figures in the attached table indicate that for the period from May 1, 1969 to the end of 1982:

-- Net increases in Treasury borrowing requirements attributable to transactions with the IMF averaged $454 million annually, compared to average annual increases in Federal borrowing of $54 billion.

-- Treasury debt <u>outstanding</u> attributable to transactions with the IMF averaged $1.6 billion annually. This is not an annual increase in Treasury borrowing, but an estimate of the average total debt outstanding each year attributable to cumulative U.S. transactions with the IMF. As of December 31, 1982, the outstanding borrowing attributable to such transactions amounted to $6.3 billion, about 1/2 of 1 percent of the total outstanding Treasury debt of $1.2 trillion.

-- Net interest costs to the Treasury associated with all U.S. transactions with the IMF averaged $42 million annually. In fiscal 1982, interest costs on total Treasury debt amounted to $117 billion.

-- Net annual valuation losses to the U.S. on the U.S. reserve position in the IMF averaged $69 million.

-- The overall net annual cost to the U.S., taking account of interest and valuation, thus averaged $111 million.

Estimated Gains and Losses Associated With U.S. Transactions Under U.S. Quota and U.S. Loans to IMF
(millions of dollars)

Year Ended April 30 1/	Cumulative Net Treasury Debt(-) or Cash(+) Position Arising From: Transactions Under U.S. Quota 2/ (1)	U.S. Loans to IMF 3/ (2)	Total 4/ (3)	Borrowing Cost(-) or Reduction(+) from Column(3) 5/ (4)	Interest Received by U.S. on Loans to IMF 6/ (5)	Remuneration Received by U.S. from IMF 7/ (6)	Valuation Gains(+) or Losses(-) on U.S. Reserve Position 8/ (7)	Interest Earned on Holdings of Foreign Currencies Drawn from IMF 9/ (8)	Total Net Gains(+) or Losses(-) 10/ (9)
1970	-716	-	-716	-50	-	+13	-	-	-37
1971	-702	-	-702	-38	-	+12	-	-	-26
1972	+445	-	+445	+19	-	*	-	-	+19
1973	+811	-	+811	+39	-	-	+34	-	+73
1974	+704	-	+704	+54	-	-	+54	-	+108
1975	-300	-	-300	-22	-	*	+70	-	+48
1976	-940	-	-940	-52	-	+9	-182	-	-225
1977	-2,695	-131	-2,826	-138	+3	+79	+54	-	-2
1978	-2,726	-639	-3,365	-197	+26	+79	+219	-	+127
1979	-1,368	-329	-1,697	-140	+28	+30	+223	+25	+166
1980	-555	-16	-571	-65	-	-	+15	+46	-4
1981	-1,294	-334	-1,628	-192	+16	+22	-203	+63	-294
1982	-3,416	-862	-4,278	-581	+88	+216	-1,134	+75	-1,336
1983 thru 12/31/82	-5,092	-1,216	-6,308	-364	+64	+222	-94	+39	-133
Total Period: 5/1/69-12/31/82				-1,727	+225	+682	-944	+248	-1,516
Annual Average	-1,306	-258	-1,564	-126	+16	+50	-69	+18	-111

Footnotes

*Indicates less than $500,000.

1/ Represents IMF fiscal year.

2/ Includes U.S. transfers of dollars to the IMF (i.e., an outflow of dollars from Treasury) and dollar balances received by the U.S. from the IMF and from sales of foreign currency drawn by the U.S. from the IMF (i.e., an inflow of dollars to the Treasury).

3/ Includes U.S. loans and repayments under the IMF's General Arrangements to Borrow and Supplementary Financing Facility.

4/ Transfers to and from the IMF under the U.S. quota subscription or U.S. lending arrangements result in budget outlays and simultaneous receipts of U.S. reserve position in the IMF; these transactions have a zero effect on net outlays and the budget deficit.

5/ Equals column 3 times average Treasury 3-month bill rate during period. Payments enter the U.S. budget as interest on the public debt; inflows reduce Treasury's need to borrow and thus reduce interest expense.

6/ Enters the U.S. budget as a receipt.

7/ Remuneration on U.S. creditor position; prior to 1975, remuneration was 1.5%, although special income distributions were made in 1970 and 1971 which raised the effective rate to 2.0 percent in those years. From 1975, the rate was based on short-term market interest rates in the five largest IMF members (U.S., U.K., Germany, France, Japan). Enters the U.S. budget as a receipt. Payments are made by IMF annually, as of April 30; FY 1983 figure represents net accrual as of December 31, 1982.

8/ Reflects changes in the dollar value of the U.S. reserve position in the IMF due to an appreciation (-) or depreciation (+) of the dollar in terms of the SDR. Enters the U.S. budget as a positive or negative net outlay.

9/ Interest earned on investments of German marks and Japanese yen acquired from U.S. drawing on IMF in November 1978. Enters the U.S. budget as part of the net profit or loss of the Exchange Stabilization Fund of the Treasury, recorded as a positive or negative net outlay.

10/ Equal to the sum of columns 4 through 8.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE February 23, 1983

RESULTS OF AUCTION OF 5-YEAR 2-MONTH NOTES

The Department of the Treasury has accepted $5,500 million of $10,944 million of tenders received from the public for the 5-year 2-month notes, Series H-1988, auctioned today. The notes will be issued March 1, 1983, and mature May 15, 1988.

The interest rate on the notes will be 9-7/8%. The range of accepted competitive bids, and the corresponding prices at the 9-7/8% interest rate are as follows:

	Bids	Prices
Lowest yield	9.94%	99.646
Highest yield	10.00%	99.406
Average yield	9.96%	99.566

Tenders at the high yield were allotted 15%.

TENDERS RECEIVED AND ACCEPTED (In Thousands)

Location	Received	Accepted
Boston	$ 12,147	$ 11,722
New York	9,160,002	4,545,057
Philadelphia	10,365	8,665
Cleveland	88,633	73,633
Richmond	48,815	24,815
Atlanta	30,123	28,848
Chicago	781,743	237,018
St. Louis	64,262	59,265
Minneapolis	8,228	8,223
Kansas City	28,463	25,188
Dallas	14,681	14,681
San Francisco	695,190	461,690
Treasury	1,661	1,661
Totals	$10,944,313	$5,500,466

The $5,500 million of accepted tenders includes $911 million of noncompetitive tenders and $4,589 million of competitive tenders from the public.

In addition to the $5,500 million of tenders accepted in the auction process, $435 million of tenders was awarded at the average price to Federal Reserve Banks as agents for foreign and international monetary authorities.

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TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE UPON DELIVERY
EXPECTED AT 1:00 P.M.

TREASURY DEPARTMENT

Address
By
Donald T. Regan
Secretary of the Treasury
before the
International Forum of the
U.S. Chamber of Commerce

Thursday, February 24, 1983

Good Afternoon.

I am delighted to be here at the Chamber where so many of the pronouncements and policy statements are so wise, far sighted and logical -- that is to say, where you agree with the Administration! Seriously, I would like to say that we in the Administration have appreciated your active interest and support over the past two years and we look forward to a close working relationship in the future.

I would like to spend the next few minutes today talking about the need for additional resources for the International Monetary Fund. Now I know this is a little like preaching to the converted. The Board of the Chamber has formally endorsed the IMF quota increase and that vote of support is very much appreciated. But the subject is one which needs much more communications and understanding.

Two weeks ago finance ministers representing 146 nations met here in Washington and hammered out a final agreement to increase the lending capacity of the IMF.

The agreed increase in IMF quotas (that is, subscription contributions to be made by the member countries) is roughly 47 percent. In dollar terms, this 47 percent increase is roughly equivalent to an increase from $67 billion to $99 billion. In addition to the quotas, there is also a special fund at the IMF and we agreed to increase that from $7 billion to about $19

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billion. The total increase for both the quotas and the GAB is roughly $43 billion with the American share of that increase being $8.4 billion.

While we in the Administration have reached agreement with our foreign friends, the arrangement must be approved by our friends on Capitol Hill. In a few days, draft legislation will be sent to Congress formally requesting approval for the American share of this increase.

I know that most of you are very familiar with all this. But, to many outside Washington, all of this may seem like a lot of government gobbledygook -- and to make matters worse its international gobbledygook. But underneath the jargon of IMF, GAB, CFF, SDR and the like, there is an issue that has a very direct impact on our own economic well being and on the American business community in particular.

As the world's central international monetary institution, the IMF makes loans to members on a temporary basis in order to safeguard the functioning of the world financial system. It provides borrowers with an extra margin of time and money which they can use to bring their payments situation back into reasonable balance in an orderly fashion ... and without being forced into abrupt and even more restrictive measures to limit imports. In addition, a borrower's agreement with the IMF on an economic program is usually viewed by the financial market as an international "seal of approval" of the borrower's policies and serves as a catalyst for additional private and official lending.

The IMF has been playing this role -- and playing it very well I might add -- for several decades. But, over the past year international debt problems and the IMF have become front page news on a regular basis. The reason is that the world economy is going through a major transitional phase and the debt problems of Argentina, Brazil, Mexico and the growing list of other nations is a manifestation of this transition. It is a complicated situation because there are at least five major components -- large scale trends, if you will -- that are taking place simultaneously.

First, there is the movement to curtail spending.

The entire world -- not just the United States -- has been on a "spending binge" for the past two decades. And we have all been riding that binge for so long that the basic way of looking at expenditures has become distorted.

The 1960s and 1970s were the decades of rising expectations. Many lesser developed countries were experiencing a heightened awareness of modernization, technology and economic growth. And there emerged a clamoring impatience for development. Aided by the thinking of a number of big spending economists in developed nations, many countries became convinced that they too could spend their way to prosperity. But the current international debt situation is stark, powerful testimony that too much spending does not bring growth and stability. If continued too long, it brings chaos.

The present state of the world economy has its roots in the inflationary pressures of the 1960's, and the twin oil shocks of the 1970's. The appropriate response to these problems should have been monetary and fiscal restraint to counter the inflationary pressures and to get those economies back on a sound footing. Instead, many countries tried to maintain real incomes at the levels that prevailed before the onset of inflation. And at the same time, they tried to preserve employment in uncompetitive industries. Reluctant to pay for these things directly, many countries resorted to debt financed increases in spending and monetization of the resulting deficits.

So by the end of 1981 total non-OPEC Developing Country debt had mushroomed to over $500 billion -- five times the level of 1973. By June of last year, the stock of debt owed to private Western Banks by non-OPEC developing countries had grown to about $265 billion, of which almost $170 billion was owed by countries of Latin America. Today Mexico and Brazil have external debts of over $80 billion dollars, Argentina's debt is probably over $40 billion and there is a long list of other nations with huge debts.

But for too many years, the world has been mesmerized by the modern day money mentality. If spending $10 billion is good, then spending $20 billion must be better.

And for too many years, nations -- including the United States -- have bought and bought and bought on a massive scale. And instead of paying, they say "Charge it."

The second trend has to do with inflation. Most economies of the world -- led by the U.S. -- are moving from high and rising inflation and interest rates to declining inflation and interest rates.

In the inflationary environment of the last decade, debtor nations were able to keep on accumulating that debt, and failed to take the adjustment measures needed to cool their overheated economies and bring external financing requirements back to sustainable levels. But with the shift to a disinflationary world economic environment, their debts have become very difficult for them to manage. Commercial banks involved in international lending took a more pessimistic view of prospects for repayment, and began to retrench sharply. As a result the borrowers have been finding it difficult if not impossible to scrape together the money to meet upcoming debt payments. As a consequence, the international financial and economic system is experiencing strains that are without precedent in the postwar era and which threaten to derail world economic recovery.

Thirdly, of course, is the recession which has contributed to slack demand for both raw materials and for finished products. Since 1980, for example, the IMF all-commodity price index declined 27 percent. Measured from 1980 to the end of last year, copper was down 32 percent; sugar -- down 80 percent; rubber -- down 43 percent.

Fourth the world economy is at the same time in the process of shifting increasingly toward the service sectors -- particularly high technology -- and away from the traditional "smoke stack" industries. Services in this country now account for about 66 percent of the gross national product and, according to the U.S. International Trade Commission, services will account for $135 billion in U.S. current account this year, a 52 percent increase over 1980. The U.S. trade balance in services rose from $3 billion in 1970 to an estimated $38 billion last year. The growth of the services and technology industries is a world-wide phenomenon and I am not certain anyone really understands the dimensions of this ongoing transition.

And finally, as if all this were not enough, we are currently witnessing some important changes in the world oil market.

On balance, a decline in oil prices is clearly to be desired. It would contribute toward economic recovery, reduce inflationary pressures, improve the external payments situation of most nations and reduce the debt problems of the oil importing LDCs.

Let me review these effects in greater detail -- using a hypothetical 10 percent fall in oil prices from last month's average of about $33 per barrel. Please be very clear: I am not predicting such a decline, but rather attempting to provide a rough unit of measurement for whatever does happen to oil prices. Generally speaking, we can assume that the effects are proportional. That is, a price reduction of 20 percent would result in roughly twice the effects.

A 10 percent cut in oil prices would lower our annual oil bill by more than 10 billion dollars. This would stimulate expansion and employment. All told, it would not be unreasonable to asume that U.S. real GNP would increase between 1/4 - 1/2 percentage points. And for the OECD countries as a whole -- which together consume over 400 billion dollars in oil -- there would be similar positive effects.

The oil-importing LDCs would benefit most dramatically. A 10 percent price cut could reduce their oil bill by 8 billion dollars. And it is worth noting that of the 10 largest LDC debtor nations, eight are oil importers.

Obviously, the big losers from an oil price decline would be the oil exporting LDCs -- the OPEC nations plus a handful of non-OPEC oil exporters. If oil prices were to remain unchanged, the OPEC nations would probably have experienced a small collective 1983 deficit on current account. With a 10 percent cut, OPEC oil export revenues would be more than $20 billion lower in the first full year following such a price decline and revenues of the four major non-OPEC oil exporters (Mexico, Egypt, Peru and Malaysia) would be lower by $2-3 billion.

As for the Arab Gulf OPEC producers, about which fears have been raised about potential disruptive effects on their investment flows, a 10 percent price cut would probably still leave them in payments surplus.

As far as the effect of the international financial system is concerned, it is generally accepted that the overall quality of banks' international loan portfolios would imporve. This would reflect the generally improved position of non-oil LDCs, even though loans to some large borrowers heavily dependent on oil exports might become more vulnerable. Indonesia, Mexico, and Venezuela are most frequently mentioned in this regard.

When all this interwoven maze of currents and cross-currents is added together, you have commodity prices which have dropped, declining demand for exports particularly from the developing nations, and high and rising debt burdens. And it is within this international economic environment that the IMF is playing such a key role in assisting nations to move through this very difficult period with a minimum disruption.

If there was too much international lending in the decade of the 70s that contributed to today's problems, too little lending in the 80s would be disasterous. The key here is to pursue a prudent and balanced approach.

Many have asked: What difference does all this make to us? To the businessman in Phoenix, or the banker in St. Louis or the housewife in Boston? The short answer is that it makes a tremendous difference, because the ability of these countries to successfully adjust to these new realities will have a direct and powerful impact on economic activity here in the United States.

U.S. exports in 1980 accounted for 19 percent of total production of goods compared to only 9 percent ten years earlier. And during the same period, export related jobs rose 75 percent, to over 5 million.

Let me cite Mexico as an immediate case in point.

Mexico is our third largest trading partner, after Canada and Japan. And, as recently as 1981, it was a partner with whom we had an export boom and a substantial trade surplus. This situation changed dramatically in 1982, as Mexico began experiencing severe debt and liquidity problems. As a result, U.S. exports to Mexico dropped by a staggering 60 percent between the fourth quarter of 1981 and the fourth quarter of 1982. Our $4 billion trade surplus with Mexico in 1981 was transformed into a trade deficit of nearly $4 billion in 1982, due mainly to an annual average drop in U.S. exports of one-third. This $8 billion deterioration was our worst swing in trade performance with any country in the world, and it was due almost entirely to the financing problem.

We believe that this situation will start to turn around, and we can begin to resume more normal exports to Mexico. If this happens, it will be due in large part to the fact that, late in December, an IMF program for Mexico went into effect. This program and the financing associated with it will permit resumption of more normal levels of economic activity and imports. Without the IMF program, all we could look forward to would be ever-deepening depression in Mexico and still further declines in our exports to that country. Improvement in the Mexican situation will translate directly into more jobs in the U.S.

And there is a second way in which all this affects us.

What if debtor nations cannot service their debts? If interest payments to U.S. banks are more than 90 days late, the banks stop accruing them on their books, they suffer reduced profits and bear the costs of continued funding of the loan. Provisions may have to be made for loss, and as loans are actually written off, the capital off the bank is reduced. In that case the creditors banks' capital/asset ratios would shrink. American banks would then have to take measures to restore the capital/asset ratios. Banks would be forced to make fewer loans to all borrowers, domestic and foreign. Auto loans in Cincinnati, housing loans in Dallas, capital expansion loans in California -- all would be affected.

There are also those who cannot understand how the Administration can endorse such a large increase for the IMF at a time when we are trying to hold the line at home on the Federal budget. But, international monetary activities should not be confused with foreign aid.

When the U.S. increases its commitment to the IMF, a "line of credit" is established which the fund may draw upon, if needed, in conjunction with commitments provided by other nations. As our line of credit is used, the U.S. receives a corresponding increase in liquid international monetary reserve assets which earn interest. Consequently, our increase in "quotas" doesn't affect budget outlays or the budget deficit, although transfers to and from the U.S. and the IMF affect Treasury borrowing.

I know there is a widespread concern that an increase in IMF resources will amount to a bank bail-out at the expense of the American taxpayer. Many would contend that the whole debt and liquidity problem is the fault of the banks -- that they've dug themselves and the rest of us into this whole through greed and incompetence, and now we intend to have the IMF take the consequences off their hands. This line of argument is dangerously misleading, and I would like to set the record straight.

First, the steps that are being taken to deal with the financial problem, including the increase in IMF resources, require continued bank involvement. Far from allowing them to cut and run, orderly adjustment requires increased bank lending to troubled borrowers that are prepared to adopt serious economic programs. That is exactly what is happening -- for example the banks will be putting more than $10 billion of new money into Argentina, Brazil, and Mexico in 1983.

It is also a mistake to think that the increase in IMF resources is coming mainly from the United States. The U.S. shares in the increase in IMF quotas is 18 percent -- which means other countries are putting up the remaining 72 percent, the great bulk of the increase. This will keep our voting share at slightly over 19 percent, which will maintain our veto over major IMF decisions and provide a needed margin of protection for the future. Some of our allies would claim that we aren't pulling our own weight -- that our stake in world trade and finance is bigger than the share of resources we are proposing to put into the IMF would indicate.

The whole debt and liquidity problem cannot fairly be said to be the fault of the commercial banks. In fact, the banking system as a whole performed admirably over the last decade, in a period when there were widespread fears that the international monetary system would fall apart for lack of financing in the aftermath of the oil shocks. The banks managed almost the entire job of "recycling" the OPEC surplus and getting oil importers through that difficult period.

The task before us now is one of education and communications -- which is where I began my remarks. I am confident that once the nature of the problem and the true role of the IMF is clearly understood, that support for the requested increase will be forthcoming.

You and your organization can play a crucial role in communicating that message and, in particular, in articulating the importance of the issue in terms of American business, American jobs and American economic prosperity.

Thank you.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

For Release Upon Delivery
Expected at 8:30 a.m. EST
February 25, 1983

STATEMENT OF
ROBERT G. WOODWARD
ASSOCIATE TAX LEGISLATIVE COUNSEL
DEPARTMENT OF THE TREASURY
BEFORE THE
SUBCOMMITTEE ON TAXATION AND DEBT MANAGEMENT
OF THE SENATE COMMITTEE ON FINANCE

Mr. Chairman and Members of the Subcommittee:

I am pleased to appear before you today on behalf of the Treasury Department to discuss the general treatment of expenses incurred by taxpayers traveling away from home on business, and the special rules in this area applicable to State legislators and Members of Congress. This discussion is intended to aid you in your consideration of S. 70, which deals with the deduction of travel expenses by Members of Congress.

Description of S. 70

S. 70 would repeal the special rule enacted in 1952 which establishes as a Member's "tax home" the Member's place of residence within the State, Congressional district or possession that the Member represents in Congress. The bill also would repeal the $3,000 limit on the amount of the deduction for living expenses incurred by Members while away from their tax homes on business.

R-2049

General Treatment of Expenses for Traveling Away From Home on Business

In general, a taxpayer may not deduct expenditures for personal, living, or family expenses. However, Internal Revenue Code section 162(a) provides an exception for ordinary and necessary expenses incurred while traveling away from home in pursuit of a trade or business. For this purpose, an individual is "away from home" only if he is traveling on business overnight or for a period sufficient to require sleep or rest.

If a taxpayer is traveling away from home on business, his deductible expenses include expenditures for transportation, meals, and lodging, together with incidental expenses such as laundry. Deductions for lodging expenses incurred away from home are appropriate to reflect a duplication or increased level of expense which the taxpayer would not incur in the absence of business necessity. Similarly, deductions for meal expenses incurred away from home are appropriate to reflect the additional expense of eating outside the home which the taxpayer incurs for business reasons.

Because an individual may only deduct living expenses incurred while away from home, it is necessary to determine the location of the individual's "tax home." Under the rules the Internal Revenue Service applies to taxpayers generally, an individual's tax home is his principal place of business.1/ If an individual conducts his business at more than one location, his principal place of business is determined on the basis of facts and circumstances. The most important considerations in making this determination are: the amount of time spent at each location; the amount of income derived at each location; and the degree of business activity at each location.

1/ At least one Circuit Court of Appeals, in deciding the locale of an individual's tax home, has framed the issue in terms of whether, based on all the facts, it would be reasonable for the taxpayer to live in the vicinity of where he is employed. See Six v. United States, 450 F.2d 66 (2d Cir. 1971). Although this approach rejects the IRS' "principal place of business" formulation, the results reached under either test would in most instances be the same.

Generally, before a deduction for travel expenses may be claimed, a taxpayer must substantiate the amount of the expense, the time and place of travel, and the business purpose of the expense. In general, the taxpayer must maintain an account book, diary, statement of expense, or similar record, together with documentary evidence, such as receipts or paid bills, for expenditures of $25 of more.

Expenditures made for political purposes, including costs of campaigning and attending political conventions, are considered nondeductible personal expenses. This rule is applicable whether or not the campaign is successful and whether or not the campaign is for a new position or for reelection to a position previously held.

State Legislators

Prior to 1976, the rules generally applicable to all taxpayers for deducting travel expenses were applied to State legislators. Most State legislators treated their residences as their tax homes for tax purposes and deducted their traveling expenses while at the State capital; however, the Internal Revenue Service often challenged these deductions. The tax home of each State legislator was thus determined on a case-by-case basis.

The tendency toward more frequent and lengthy State legislative sessions often made it unclear whether the legislator's tax home was the State capital or his home district. In some cases, the legislator's tax home would shift from year to year. This, in turn, caused recordkeeping difficulties for legislators as they tried to provide the required substantiation for travel expenses without knowing the location of their tax homes in advance.

In recognition of this problem, special temporary rules for State legislators were enacted as part of the Tax Reform Act of 1976. Under these rules, a State legislator could elect as his tax home his place of residence within the legislative district which he represented. He thus could claim deductions for transportation costs and living expenses incurred while away from his home district. The deductible living expenses could be claimed without substantiation. The amount was computed by multiplying the legislator's total number of "legislative days" for the year by the per diem amount generally allowable to Federal employees for travel away from home. For this purpose, "legislative days" included (1) days in which the legislature was in session (including any day in which the legislature was not in session for 4 consecutive days or less, i.e., weekends) and (2) days on which the legislature was not in session but the legislator attended a meeting of a legislative committee.

Revenue Ruling 82-33, 1982-10 I.R.B. 4, holds that for purposes of these rules the "generally allowable" Federal per diem is the maximum Federal per diem authorized for the seat of the legislature. The Federal per diem travel allowance is $50 for most areas of the United States but is higher for certain high cost areas, including a number of State capitals.

In 1981 the temporary elective provisions for State legislators were modified and made permanent. The amendments increased the amount of the deduction allowed per day without substantiation to the greater of (i) the amount generally allowable to Federal employees in travel status or (ii) the amount generally allowable by the State to its employees for travel away from home, up to 110 percent of the appropriate Federal per diem.

A second amendment made in 1981 created a conclusive presumption that a legislator was away from home on business on each legislative day. This amendment reversed the decision of the Tax Court in Chappie v. Commissioner, 73 T.C. 823 (1980), which affirmed the Internal Revenue Service's position that a State legislator must comply with the normal rules requiring a taxpayer to be "away from home" in order to deduct living expenses.

The third amendment made in 1981 excluded from application of the elective provisions any State legislator whose place of residence within his legislative district is 50 or fewer miles from the State capitol building.

Members of Congress

Members of Congress, like other business travelers, are entitled to deduct ordinary and necessary travel expenses incurred in pursuit of their trade or business as a representative of their legislative districts. One of the first issues to arise in connection with the deductibility of a Member's travel expenses involved the location of a Member's tax home.

In a 1936 decision, the Board of Tax Appeals held on the facts presented that the "tax home" of one particular Member of Congress was the District of Columbia. Lindsay v. Commissioner, 34 B.T.A. 840 (1936). Under this decision, Members of Congress were generally not permitted to deduct any of their living expenses while at the nation's capital. Subsequently, in 1952, Congress reversed the rule in Lindsay and amended the predecessor of Code section 162 to provide that a Member's tax home shall be his or her residence in the district he or she represents. The Senate Report explained that the amendment was intended "to permit the Members of Congress to claim deductions for tax purposes to the same extent as other persons whose business or profession requires absence from 'home' for varying periods of time." S. Rept. 1828, 82d Cong., 2d Sess., reprinted in 1952-2 C.B. 374. In addition, allowable deductions for living expenses incurred by Members while away from their tax homes on business were limited to $3,000 per year.

In 1981 Congress made three amendments to the rules affecting the tax treatment of living expenses of Members in the Washington, D.C. area. First, the $3,000 cap on deductible expenses was eliminated. Second, section 280A of the Code was amended to provide an exception to the general rule which denies business expense deductions with respect to any dwelling unit used by a taxpayer or his family for personal purposes for more than 14 days a year. Under this amendment, the general rule does not apply in cases where the residence is used by the taxpayer while away from home on business. Third, section 280A was further amended to direct the Treasury Department to prescribe amounts deductible, without substantiation, for a Member's living expenses while away from home in the District of Columbia area. Pursuant to this directive, Treasury promulgated regulations in January 1982 setting forth a series of rules which were patterned after the rules applicable to State legislators.

As part of the Urgent Supplemental Appropriations Act of 1982, Congress repealed two of the three 1981 amendments affecting the deductibility of living expenses by Members of Congress. The 1982 legislation restored the $3,000 cap on deductible living expenses incurred by Members of Congress while away from their tax homes on business. The legislation also repealed the special rule permitting Members to deduct designated amounts prescribed by Treasury regulations for living expenses without substantiation. The 1982 legislation did not affect the 1981 amendment to section 280A that provided an exception for deductions with respect to dwelling units used by taxpayers while away from home on business. The 1982 legislation is effective for taxable years beginning after December 31, 1981.

This concludes my prepared remarks. I will be happy to respond to any questions that you may have.

TREASURY NEWS

partment of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE February 25, 1983

TREASURY OFFERS $9,000 MILLION OF 45-DAY
CASH MANAGEMENT BILLS

The Department of the Treasury, by this public notice, invites tenders for approximately $9,000 million of 45-day Treasury bills to be issued March 7, 1983, representing an additional amount of bills dated April 22, 1982, maturing April 21, 1983 (CUSIP No. 912794 CB 8).

Competitive tenders will be received at all Federal Reserve Banks and Branches up to 1:30 p.m., Eastern Standard time, Wednesday, March 2, 1983. Wire and telephone tenders may be received at the discretion of each Federal Reserve Bank or Branch. Each tender for the issue must be for a minimum amount of $1,000,000. Tenders over $1,000,000 must be in multiples of $1,000,000. The price on tenders offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Noncompetitive tenders from the public will not be accepted. Tenders will not be received at the Department of the Treasury, Washington.

The bills will be issued on a discount basis under competitive bidding, and at maturity their par amount will be payable without interest. The bills will be issued entirely in book-entry form in a minimum denomination of $10,000 and in any higher $5,000 multiple, on the records of the Federal Reserve Banks and Branches. Additional amounts of the bills may be issued to Federal Reserve Banks as agents for foreign and international monetary authorities at the average price of accepted competitive tenders.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m., Eastern time, on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e. g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Those submitting tenders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Settlement for accepted tenders in accordance with the bids must be made or completed at the Federal Reserve Bank or Branch in cash or other immediately-available funds on Monday, March 7, 1983.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars may be obtained from any Federal Reserve Bank or Branch.

TREASURY NEWS
partment of the Treasury • Washington, D.C. • Telephone 566-204

For Release Upon Delivery
Expected at 10 a.m. EST
February 28, 1983

STATEMENT OF
J. GREGORY BALLENTINE
DEPUTY ASSISTANT SECRETARY (TAX ANALYSIS)
DEPARTMENT OF THE TREASURY
BEFORE THE SUBCOMMITTEE ON OVERSIGHT
OF THE
HOUSE COMMITTEE ON WAYS AND MEANS

Mr. Chairman and Members of the Subcommittee:

I am pleased to have the opportunity to appear before you today to discuss Federal contract leasing practices in general and the Navy TAKX program in particular.

In General

I would like to begin my testimony by describing briefly a typical type of leasing transaction which is commonly called a "leveraged lease." A leveraged lease generally involves three parties: a lessor, a lessee, and a lender to the lessor. In the usual case, the lessor will purchase the property to be leased, financing the acquisition with a downpayment of (say) 30 percent of the cost of the property, and borrowing the balance from a third party lender. The property is then leased to the lessee on a net lease basis (i.e., the lessee has agreed to bear the everyday operating costs of the property) for a term that covers a substantial part of the useful life of the property. The lessee's rental payments to the lessor, together with the expected residual value of the property at the end of the lease plus the anticipated tax benefits on the property, are generally sufficient to discharge the lessor's payments to the lender, repay the lessor's investment and provide the lessor a reasonable return on that investment. If the transaction is considered a "true" lease for Federal tax purposes, the lessor will be considered the owner of the property. In that event the lessor will be entitled to claim the investment tax credit and cost recovery deductions attributable to the property and will be required to report the lessee's payments as rental income.

If the transaction fails to qualify as a true lease for Federal tax purposes, the purported lessee would be treated as the owner of the property and the purported lessor would be viewed as merely financing the lessee's purchase of the property. In that case the lessor would not be entitled to any investment tax credit or cost recovery deductions with respect to the property. Any amount received by the lessor as "rent" under the agreement generally would be considered payments of the sales price of the property, on which the lessor may have gain or loss. The lessee would not be entitled to any rental deductions for payments under the agreement, but would instead acquire a basis in the property generally equal to the principal amount payable over the term of the agreement. In addition, as the property's owner, the lessee would be entitled to claim any investment credit or cost recovery deductions allowable with respect to the property.

The determination of whether a transaction which is a lease in form is in fact a lease for Federal tax purposes or whether it is a conditional sale or other form of financing arrangement will depend on the facts of the particular case. The issue of a transaction's status as a lease or a mere financing arrangement has been litigated many times. There are no definitive criteria used for categorizing such transactions under current law. In the case of Frank Lyon Co. v. United States 1/, the Supreme Court stated that a transaction will be treated as a true lease for tax purposes where "the lessor retains significant and genuine attributes of the traditional lessor status." The Court went on to explain, however, that "what those attributes are in any particular case will necessarily depend on its facts."

Revenue Procedure 75-21

While no specific formula for a true lease exists, in 1975 the Internal Revenue Service published Revenue Procedure 75-21 2/ which contains a set of guidelines

1/ 435 U.S. 561 (1978).

2/ 1975-1 C.B. 715.

indicating the conditions under which the Service will issue advance rulings requested by interested taxpayers on whether certain transactions are true leases of property for Federal tax purposes. These guidelines, which have been supplemented and amended several times, do not (and are not intended to) define the factors necessary to having a true lease for Federal tax purposes. Rather, they merely outline the circumstances under which the Service will issue an advance ruling. Indeed, there are a number of court decisions upholding the parties' characterization of a transaction as a lease even though the transaction would have failed to meet the conditions of the Service's guidelines.

In general, before the Service will issue an advance ruling on the status of a leasing transaction, the guidelines require (i) that the lessor have, and maintain throughout the lease term, a minimum "at risk" investment in the property equal to 20 percent of the property's cost; (ii) that the residual value of the property at the end of the lease term be equal to at least 20 percent of its cost; and (iii) that the property have a remaining useful life of 20 percent of its originally estimated useful life. In addition, the lessor must show that it expects to receive a profit from the transaction exclusive of tax benefits. The guidelines also restrict the use of options allowing the lessee to purchase the property for less than the property's fair market value, and the use of lessee loans to the lessor or guarantees of any indebtedness incurred by the lessor to purchase the property.

<u>Service Agreements</u>

Service contracts or agreements, as such, are not expressly dealt with in Revenue Procedure 75-21. The use of service contracts has significance for Federal tax purposes in cases where a direct lease of the property to its ultimate user would limit the amount of tax benefits available to the owner of the property. For example, under section 48(a)(5) of the Internal Revenue Code, the direct use of property by a governmental unit or tax exempt entity under a lease agreement would generally operate to disallow any investment tax credit otherwise available with respect to the property. In contrast, if the parties enter into a valid service agreement under which the owner itself will use the property in performing services for the governmental unit or tax exempt entity, the investment tax credit limitation may be avoided.

In a typical lease, a lessor will transfer possession and control of the property to the lessee for the term of the lease, and the lessee will be responsible for its day-to-day operation. In contrast, under a valid service agreement, the ultimate user of the property may be able to direct when and where the property is to be used; but control, possession, and day-to-day operation of the property remain with the supplier of the service.

Whether an agreement is a service contract or a lease is an inherently factual determination. The Service has issued several published and private rulings on attempts to use service agreements to avoid the investment tax credit limitation in section 48(a)(5). In one ruling the IRS concluded that rental agreements under which copying machines were placed with tax exempt organizations and governmental units were not service contracts (thus ruling that the machines did not qualify for the investment credit), reasoning that the supplier of the equipment had given up possession and use of the equipment to such an extent that the user was able to provide services for itself. 3/ This conclusion was later rejected by the Court of Claims in Xerox Corp. v. United States 4/ where the court interpreted the facts differently and held that the taxpayer "was providing a service to its customers under the rental agreements with the machines an integral part of this service."

Navy Program

You have asked us to comment on whether the IRS would characterize the Navy Department's "convert and charter program" for one of its 13 TAKX ships as a valid lease and service contract. The transaction, very simply, is structured as a net lease of the ship by an investor partnership as lessor to an unrelated corporation as lessee. The lessee, in turn, will time charter the vessel to the Navy Department under a time charter party. The initial period of the time charter is for 5 years with 4 successive options for the Navy to renew the charter agreement for 5 years each.

Although the IRS has reviewed the agreements relating to the Navy transaction that were supplied by the Subcommittee, it would need more information before it could

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3/ Rev. Rul. 71-397, 1971-2 C. B. 63.

4/ 656 F.2d 659 (1981).

render its opinion on the validity of the lease (the bareboat charter) and service contract (the time charter). But even if the Service possessed all the relevant facts, the Service could not express an opinion publicly on the transaction since the transaction involves known taxpayers. However, it should be noted that the IRS has ruled favorably on similar arrangements in the past, although each case is different and must stand on its own facts.

Tax Indemnification Agreement

You have also requested that we comment on the tax indemnification provision included within the "Time Charter Party" agreement.

In a typical lease arrangement, the rents charged are a function, among other factors, of the tax benefits attributable to the leased property that may be available to the lessor. In other words, the availability of the tax benefits on the leased property are an essential component of the lessor's return on the transaction. If the transaction ultimately is found to be a mere financing transaction rather than a valid lease, any tax benefits will be available to the lessee rather than the lessor. It is not uncommon, therefore, for a lease agreement to provide that the lessee will indemnify the lessor against the loss of the anticipated tax benefits.

In the Time Charter Party, the Navy Department has agreed to indemnify the ship's owner, under certain circumstances, for the loss of cost recovery deductions and the investment tax credit with respect to the ship. This provision appears to be consistent with the normal business practice of insuring that the benefit of the bargained for tax deductions and credits are available as anticipated by the parties.

Government Leasing

I will now discuss the economics of government leasing with particular emphasis on the role of financing costs and correct, consistent budget accounting for private capital formation incentives.

One financial aspect of Government lease arrangements generally substitutes private financing for Federal borrowing. Since the Federal Government can always borrow at lower rates than private borrowers, this financial aspect favors Government purchases with Federal borrowing over leasing. I should like to stress, however, there frequently are other financial aspects of a lease arrangement or other cost or policy advantages that can make leasing the preferred alternative.

It is helpful to distinguish two kinds of fact situations concerning the use by the government of durable capital goods. In one situation, the legal arrangements combine the leasing of durable goods with a contract for services not necessarily or customarily performed by the government. In such cases, the rental or lease charges are only partially determined by the capital costs comprising the "net lease" terms I have described above; management and other costs of producing the services associated with the capital goods loom larger. Frequently, in these situations, evaluation of the management and other cost differentials as between government ownership and leasing are closely, if not inextricably, combined with the "lease-buy" choice. Indeed, in view of the discipline of competition to which private ownership and management of this kind of assets is subject, in this fact situation there may well be an efficiency presumption favoring leasing over government ownership and management.

In contrast, the other fact situation concerns those instances in which few if any services associated with the asset are contracted for, or, if there are associated services, these are of a kind customarily performed by government. In these cases, the only relevant aspect of the lease-buy choice is the difference in financing method. Whether the government leases or buys, it will ultimately manage the asset in the same way, incurring the same operating and maintenance costs, and deriving the same flow of services. In such a fact situation a major difference in budget cost as between buying or leasing becomes financing cost. Even in this situation other cost advantages may make leasing the more attractive alternative.

In general, because Federal Government loans are perceived by lenders to be virtually riskless, the government enjoys a borrowing rate lower than that of private parties. Moreover, due to the unavoidability of certain transaction costs inherent in Federal loan guarantees, private borrowing rates even on guaranteed loans range up to 150 basis points (1.5 percentage points) higher than on direct government borrowing. Thus, under a leasing arrangement with the government which in effect guarantees the lessor's own loan to finance the acquisition of the asset to be leased, the cost of funds will be higher than if the government purchased the asset and financed the purchase by borrowing. In these instances in which there is no question of managerial difference and no other financial lease advantage, the lower government cost of funds yields a predisposition favoring outright government ownership over leasing. Government ownership avoids incurring fundraising transaction costs that are unnecessary to accomplish the government objective that will be served by the capital good.

Of course, in the real world of government operations, the task of distinguishing those fact situations in which there is a presumption in favor of leasing from those in which the presumption favors outright government ownership is not an easy one. Other policy objectives of government may be served on occasion by a leasing arrangement that justifies somewhat higher financing costs; and differences in budgetary tracks for procurement and operation and maintenance programs may cause leases at particular times to result in real cost savings that more than offset higher financing costs. For example, the TAKX charter periods were structured in 5-year periods which gives the Navy the flexibility to terminate the contracts if our defense needs change without the U.S. Government bearing a potentially substantial loss on the residual value of the ship. Therefore, I question whether there can be a simple policy favoring or disfavoring leasing by government. Rather, the need is for procedures and techniques for evaluating lease-buy choices, a subject to which the remainder of my remarks is addressed.

Demonstration of the intuitively obvious truth that leasing, per se, cannot reduce the government's cost of obtaining the use of durable capital goods is complicated by budgeting conventions. The unified budget is fundamentally a document summarizing cash inflows and outflows, and, therefore, does not lend itself to portrayal of the annual costs of service from durable assets. In particular, budget accounting for obligational authority and outlays does not distinguish between a single capital outlay to provide services for many fiscal years and other outlays to cover a single year's service.

If the government invests in a ship that is expected to provide a stream of military services over, say, 25 years, the cost of acquiring that ship--$184 million in the case before you--appears in the budget as that much obligational authority in the year in which it is appropriated and as outlays during the year(s) in which the procurement occurs. However, it can be shown that for particular assumptions as to the 25-year stream of effectiveness and government borrowing cost, if the annual costs could be shown as lease rentals, they would be $20.3 million a year. At the government's borrowing rate, which is the budget cost of shifting payments over time, this stream of annual outlays would be exactly equivalent to the $184 million (single year) outlay in terms of social cost. Moreover, accounting for the cost of the ship as a $20.3 million outlay annually has the additional valuable attribute of correctly distributing its full cost over the 25 years of that ship's service to the country.

Thus, leasing could actually contribute to better budgetary control of government programs. If a lease arrangement yields a set of annual lease rental costs that approximately matches the expected stream of services to be realized from the leased asset and which, when discounted, costs no more than outright purchase, then leasing rather than outright purchase has the virtue of distributing budget costs to be financed by taxes among successive generations of taxpayers who enjoy the benefits. The same result might be achieved, for example, if government agencies contemplating the acquisition of durable assets were required to finance the purchase through the Federal Financing Bank under an agreement by which they obligate themselves to service and retire the debt thus incurred over the period the asset will be in productive service. The annual budget charge for debt service and retirement under such an arrangement would be, of course, substantively the same as a lease rental; but since the annual charge would reflect the government borrowing rate, budget cost would be minimized. The potential benefit of leasing for the budgetary process has been recognized by OMB in Circulars A-94 and A-104 which provide guidance in the selection of a discount rate and for evaluating the choice whether to lease or buy.

However, there are additional problems posed by budget accounting conventions that confound evaluation of potential government leases by simply discounting proposed lease rentals at the guideline government borrowing rate. These problems, to which I now turn, will invariably cause an understatement of the budget cost of leasing. If these problems are not carefully resolved, they will not only bias the lease-buy choice in favor of leasing, they may lead to the acceptance of leases that impose higher costs than outright purchase and that nevertheless understate program costs.

These budget accounting problems are rooted in provisions of the income tax laws that have been designed to encourage private capital formation. Specifically, the Investment Tax Credit (ITC) and Accelerated Cost Recovery System (ACRS) reduce the private cost of acquiring and using assets. These incentives were introduced to help offset the income tax deterrence to private capital formation. Since in a "true" lease arrangement the lessor will receive the ITC and can depreciate his asset using the ACRS schedule, the effect of these incentives is to reduce the lease rentals a private lessor must charge to recover his own investment in the asset and to earn his rate of return. When the government is the lessee, it pays these lower rentals, which will appear as outlays, but the budget will not associate with the program supported by these lease rentals the reduction in tax revenues which made these lower budget outlays possible. I shall illustrate the nature of these problems in the case of the ITC and ACRS.

The ITC operates to reduce the private cost of acquiring a qualified asset in much the same way as does a capital grant. The ITC therefore proportionately reduces any lease rentals that must be charged. If the ITC were paid directly to the owner with appropriated funds, the amount of the grant would appear in the budget among the outlays and would be associated with the program that is thus supported. But since the ITC is taken as a credit against income tax otherwise due, the budget effect is merely a reduction in tax deposits (receipts) and is not associated with the program it supports. Proper evaluation of a government lease therefore requires that account be taken of the ITC allowed the lessor at the beginning of the lease term by effectively adding the ITC to the rental stream being discounted.

Accelerated cost recovery with respect to the portion of the asset's cost representing the owner-lessor's own investment of private funds affords him the benefit of tax deferral. For example, the Navy lease of cargo ships which you are reviewing extends for 25 years. Twenty-five years is thus the period over which the lessor would predicate recovery of his recoverable costs in determining his annual lease rental charges, yet the ACRS provisions of the Code permit him to recover this in tax deductions during the first 5 years of the ship-lease term. As a consequence, the lessor will deposit less tax during the first 5 years of the lease contract, more during the remaining 20 years, hence the descriptive term "tax deferral." The present value of this tax deferral will reduce the lessor's required lease payments, but that present value, like the value of the ITC, must be added to the government's rental stream to calculate the true cost of the lease to the government. 5/

Obviously, if the full budgetary consequences of lease rentals on both the outlay and revenue side of the budget are accounted for and discounted at the government borrowing rate, the choice whether to lease or buy will hinge on the total cost to the Government under the two alternatives. This total cost will include tax costs, financing costs, and any other cost differences.

In those cases in which government leasing is justified, the budget cost of the lease can be minimized if the private financing is arranged through the Federal Financing Bank, which is authorized to finance government guaranteed obligations. I understand that Navy Department officials are inquiring into these possibilities with regard to the leases under review.

The particular characteristic of this analytical accounting of government leasing costs that I should like to call to your attention is that it computes all amounts as "pre-tax," or market price magnitudes. This follows the convention used in both our national accounts and budgeting which takes market prices as the measure of both product (GNP) and income payments, or shares. In budgeting, the rationale for using pre-tax magnitudes is that, on the expenditure side, these represent the opportunity costs of the resources devoted to public purposes; on the revenue side, pre-tax magnitudes represent the share of national product taken as taxes. Thus, the adjustments to lease rentals I have suggested above simply perform the function

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5/ Present values never appear in budgets, only annual cash flows. Thus, when tax is deferred, tax deposits diminish and increase the deficit, in the same manner as net lending. In later years, as the deferral is repaid (assuming no new investment to generate deferrals), tax deposits rise. The present value of the deferrals exceeds that of the repayments, and this may be likened to positive "average" tax deferral over the life of the lease. Naturally, this average deferral implies some net average government borrowing. The deferral benefit is therefore the interest avoided by the lessor, the consequences of which are interest payment outlays.

of expressing the full resource costs of government leases in terms that are consistent with other expenditures, including procurement of an item that might be leased.

Consistent with the correct use of pre-tax values, the form of analytical accounting for leases I have outlined does not include offsets for the taxes on the income earned by lessors and their lenders. That is, just as the cost of hiring a government employee is not reduced by the taxes that employee will pay, the income paid to lessors should not be reduced by the taxes they pay on that income. The only tax amounts that should be included in the evaluation of the lease are those that are unique to the lease transaction as opposed to government purchase and borrowing. Those are the value of the ITC and the tax deferral value of ACRS. This procedure is in accordance with the general reason for maintaining government and national accounts in pre-tax magnitudes, namely, so that the sum of government and private sector activity will represent the national product (GNP).

Conclusion

There are six basic points made in my testimony:

(1) Whether or not specific transactions are characterized for tax purposes as a lease or a financing transaction is a factual issue that cannot be determined without an examination of all the details of the purported lease arrangement.

(2) Similarly, whether or not a specific transaction is a valid service contract for tax purposes is a factual issue that cannot be determined without an examination of all the details of the agreement.

(3) Since the transactions in question involve known taxpayers neither the Treasury nor the IRS can comment publicly on their validity.

(4) To the extent that a lease arrangement simply involves substituting private financing for public financing, it is more costly than a direct purchase.

(5) In many cases other cost and policy advantages can dominate any additional financial costs of leasing.

(6) Proper accounting for the costs of a Government lease arrangement must include the revenue cost from allowing the Investment Tax Credit and the deferral advantage of ACRS.

This concludes my remarks and I will be happy to respond to any questions you may have.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
February 25, 1983

CONTACT: Robert Don Levine
(202) 566-2041

Secretary Regan Announces Treasury Executive Institute

Secretary of the Treasury Donald T. Regan today announced the establishment of the Treasury Executive Institute which will provide developmental services to Senior Executive Service (SES) executives and candidates to support achievement of their organizational and individual goals.

The Institute will use management seminars, cross-bureau assignments and department-wide task forces to deal with specific problems.

Secretary Regan said in a memorandum to Treasury Department bureaus that, "It is my hope that the Institute will become a vehicle for more than just traditional executive development activities. It is my belief that we often miss many of the opportunities to share the innovations bureaus are experimenting with and implementing -- many of which can have applications in other bureaus."

The operation of the Institute will be under the direction of a Treasury Career Advisory Panel composed of senior Treasury career officials.

Chairing the Panel for the first six months of the Institute's existence will be James I. Owens, Deputy Commissioner, Internal Revenue Service. Others serving on the Panel will be Stephen E. Higgins, Acting Director, Bureau of Alcohol, Tobacco and Firearms, H. Joe Selby, Senior Deputy Comptroller for National Operations, Office of the Comptroller of the Currency, Alfred R. DeAngelus, Deputy Commissioner, U.S. Customs Service, Robert J. Leuver, Acting Director, Bureau of Engraving and Printing, David W. McKinley, Acting Director, Federal Law Enforcement Training Center, Margery Waxman, Deputy General Counsel, William E. Douglas, Commissioner, Bureau of Government Financial Operations, Larry E. Rolufs, Deputy Director, Bureau of the Mint, W. M. Gregg, Acting Commissioner, Bureau of the Public Debt, Steven R. Mead, Executive Director, U.S. Savings Bonds Division, John R. Simpson, Director, U.S. Secret Service, and David S. Burckman, Director of Personnel, Department of the Treasury.

R-2052

Diane Herrmann, Director, Office of Equal Opportunity Program, will serve for the first six months as the Executive Director. She will be responsible for managing the day-to-day operations of the Institute.

The Treasury Career Advisory Panel will meet for the first time on Monday, February 28th to organize the Institute's work. The Institute will be financed out of the budgets of participating bureaus.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE   February 28, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $6,207 million of 13-week bills and for $ 6,200 million of 26-week bills, both to be issued on March 3, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing June 2, 1983			:	26-week bills maturing September 1, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	98.008 a/	7.880%	8.17%	:	96.011	7.890%	8.36%
Low	97.983	7.979%	8.28%	:	95.968	7.975%	8.45%
Average	97.992	7.944%	8.24%	:	95.982	7.948% 2/	8.42%

a/ Excepting 2 tenders totaling $1,355,000.

Tenders at the low price for the 13-week bills were allotted 24%.
Tenders at the low price for the 26-week bills were allotted 72%.

TENDERS RECEIVED AND ACCEPTED (In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 35,150	$ 35,150	:	$ 106,465	$ 51,465
New York	11,018,050	4,835,050	:	11,612,650	4,656,650
Philadelphia	25,545	25,545	:	14,760	14,760
Cleveland	60,895	35,895	:	78,510	73,510
Richmond	50,985	44,485	:	42,360	42,360
Atlanta	49,050	49,050	:	64,035	64,035
Chicago	1,019,080	527,080	:	740,210	283,210
St. Louis	50,230	43,230	:	56,750	44,750
Minneapolis	7,780	7,780	:	37,400	37,400
Kansas City	40,190	40,190	:	50,220	47,300
Dallas	25,365	25,365	:	17,845	17,845
San Francisco	842,315	320,315	:	1,172,870	647,860
Treasury	217,525	217,525	:	219,305	219,305
TOTALS	$13,442,160	$6,206,660	:	$14,213,380	$6,200,450
Type					
Competitive	$11,310,300	$4,074,800	:	$11,921,470	$3,908,540
Noncompetitive	854,275	854,275	:	654,510	654,510
Subtotal, Public	$12,164,575	$4,929,075	:	$12,575,980	$4,563,050
Federal Reserve	1,209,385	1,209,385	:	1,200,000	1,200,000
Foreign Official Institutions	68,200	68,200	:	437,400	437,400
TOTALS	$13,442,160	$6,206,660	:	$14,213,380	$6,200,450

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 8.163%.

R-2053

FOR IMMEDIATE RELEASE FEBRUARY 14, 1983

The Treasury announced today that the 2-1/2 year Treasury yield curve rate for the five business days ending February 14, 1983, averaged 9.90 % rounded to the nearest five basis points. Ceiling rates based on this rate will be in effect from Tuesday, February 15, 1983 through Monday, February 28, 1983.

Detailed rules as to the use of this rate in establishing the ceiling rates for small saver certificates were published in the Federal Register on July 17, 1981.

Small saver ceiling rates and related information is available from the DIDC on a recorded telephone message. The phone number is (202)566-3734.

Approved ______________________

Francis X. Cavanaugh, Director
Office of Government Finance
& Market Analysis

federal financing bank NEWS
WASHINGTON, D.C. 20220
Press inquiries: 202-566-2615

FOR IMMEDIATE RELEASE February 28, 1983

FEDERAL FINANCING BANK ACTIVITY
November and December 1982

Francis X. Cavanaugh, Secretary, Federal Financing Bank (FFB), announced the following:

FFB holdings of obligations issued, sold, or guaranteed by other Federal agencies on December 31, 1982 totaled $126.4 billion, an increase of $0.7 billion over the November 30 level. FFB increased holdings of agency debt issues by $0.3 billion and holdings of agency guaranteed debt by $0.8 billion. Holdings of agency assets purchased decreased by $0.4 billion. In November, FFB had increased its holdings by $0.6 billion to $125.7 billion, including $0.1 billion of agency debt issues and $0.6 billion of guaranteed issues. Agency assets held by FFB decreased by $0.01 billion in November. A total of 307 disbursements were made during December, compared with 283 disbursements in November.

Attached to this release are tables presenting FFB loan activity and new FFB commitments to lend during November and December and tables summarizing FFB holdings as of November 30 and December 31, 1982.

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R-2054

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
ON-BUDGET AGENCY DEBT					
TENNESSEE VALLEY AUTHORITY					
Note #269	11/12	$ 45,000,000.00	1/6/83	8.381%	
Note #270	11/19	125,000,000.00	1/6/83	8.784%	
Power Bond 1982 E	11/19	200,000,000.00	11/30/12	10.725%	
Note #271	11/30	75,000,000.00	3/3/83	8.483%	
NATIONAL CREDIT UNION ADMINISTRATION					
Central Liquidity Facility					
Note #129	11/1	72,907.00	1/31/83	8.259%	
Note #130	11/3	1,500,000.00	12/3/82	8.206%	
Note #131	11/3	2,228,161.00	12/30/82	8.206%	
Note #132	11/5	720,000.00	2/3/83	8.106%	
Note #133	11/9	750,000.00	2/3/83	8.364%	
+Note #134	11/15	2,000,000.00	12/15/82	8.670%	
+Note #135	11/15	11,613,000.00	2/14/83	8.670%	
Note #136	11/17	1,432,126.00	12/30/82	8.795%	
+Note #137	11/18	2,000,000.00	2/16/83	8.763%	
+Note #138	11/18	5,000,000.00	2/16/83	8.763%	
+Note #139	11/22	7,013,000.00	2/21/83	8.364%	
Note #140	11/29	14,450,000.00	1/28/83	8.291%	
AGENCY ASSETS					
DEPARTMENT OF HEALTH & HUMAN SERVICES					
Medical Facilities Loans					
Series G	11/19	3,014,497.00	7/1/97	10.583%	
GOVERNMENT - GUARANTEED LOANS					
DEPARTMENT OF DEFENSE - FOREIGN MILITARY SALES					
Philippines 7	11/1	102,300.62	9/10/87	10.359%	
Ecuador 5	11/3	816,879.50	8/1/85	10.284%	
Egypt 3	11/3	101,723,030.97	6/15/12	10.770%	
Israel 8	11/4	1,360,356.01	9/1/09	10.651%	
Israel 13	11/4	6,810,910.44	2/16/12	10.680%	
Kenya 10	11/5	2,219,470.00	5/5/94	10.469%	
Korea 15	11/5	170,351.00	12/31/93	10.454%	
Somalia 1	11/5	1,015,073.00	9/1/92	10.459%	
Turkey 11	11/5	485,996.95	12/22/10	10.615%	
Jordan 7	11/8	3,821,611.18	3/16/90	10.360%	
Jordan 8	11/8	1,382,880.00	11/22/90	10.414%	
Philippines 7	11/8	1,585,726.43	9/10/87	10.085%	
Tunisia 11	11/8	542,403.16	5/5/92	10.519%	
Turkey 11	11/8	87,310.32	12/22/10	10.675%	
Jordan 7	11/9	46,195.80	3/16/90	10.448%	
Israel 8	11/10	1,881,949.00	9/1/09	10.622%	
Israel 13	11/10	13,095,386.67	2/16/12	10.616%	
Cameroon 4	11/12	149,850.00	3/14/87	10.065%	
Cameroon 5	11/12	1,500,000.00	1/15/88	10.189%	
Egypt 3	11/12	625,595.14	6/15/12	10.584%	
Honduras 9	11/12	2,211,418.88	9/20/94	10.594%	
Indonesia 7	11/12	172,310.60	3/20/90	10.367%	
Kenya 9	11/12	236,692.00	3/15/93	10.492%	
Korea 15	11/12	288,441.00	12/31/93	10.526%	
Peru 7	11/12	500,841.00	2/15/88	10.204%	
Spain 5	11/12	763,853.18	6/15/91	10.426%	
Thailand 3	11/12	21,613.00	9/20/84	9.521%	
Ecuador 5	11/15	371,153.00	5/25/88	10.334%	
Greece 14	11/15	263,750.00	4/30/11	10.674%	
Honduras 9	11/15	998,582.50	9/20/94	10.693%	

+Rollover

NOVEMBER 1982 ACTIVITY

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual	INTEREST RATE (other than semi-annual)
DEPARTMENT OF DEFENSE - FOREIGN MILITARY SALES (Cont'd)					
Turkey 9	11/15	$ 6,486,959.21	6/22/92	10.619%	
Israel 13	11/16	6,035,536.46	2/16/12	10.752%	
Israel 8	11/19	51,837,000.00	9/1/09	10.571%	
Israel 13	11/19	7,484,230.43	2/16/12	10.559%	
Egypt 3	11/22	151,986,269.69	6/15/12	10.528%	
Turkey 11	11/22	728,884.93	12/22/10	10.532%	
Honduras 6	11/22	56,998.37	4/25/91	10.410%	
Israel 8	11/23	2,449,974.53	9/1/09	10.556%	
Israel 13	11/23	7,288,910.90	2/16/12	10.555%	
Turkey 11	11/24	6,584.18	12/22/10	10.647%	
Philippines 7	11/26	39,718.54	9/10/87	10.032%	
DEPARTMENT OF ENERGY					
Synthetic Fuels Guarantees - Non-Nuclear Act					
Great Plains Gasification Assoc. #36	11/1	5,000,000.00	7/1/02	11.683%	
#37	11/8	13,000,000.00	1/3/83	8.856%	
#38	11/15	15,500,000.00	1/3/83	9.204%	
#39	11/22	14,000,000.00	7/1/02	11.331%	
DEPARTMENT OF HOUSING & URBAN DEVELOPMENT					
Community Development Block Grant Guarantees					
Owensboro, KY	11/5	27,855.60	9/1/83	9.005%	9.163% ann.
Jefferson County, KY	11/9	309,197.00	11/30/83	9.395%	9.616% ann.
Lawrence, MA	11/9	40,000.00	1/1/83	8.364%	
Owensboro, KY	11/9	281,379.49	9/1/83	9.235%	9.398% ann.
Hammond, IN	11/26	45,084.00	5/1/84	9.615%	9.846% ann.
Washington County, PA	11/26	23,975.00	8/1/83	8.975%	9.083% ann.
Louisville, KY	11/30	1,320,000.00	11/30/84	9.869%	10.112% ann.
Public Housing Notes					
Sale #27	11/5	25,167,489.42	11/1/04-11/1/18	10.746%	11.035% ann.
NATIONAL AERONAUTICS AND SPACE ADMINISTRATION					
Space Communications Company	11/22	8,000,000.00	10/1/92	10.459%	10.732% ann.
RURAL ELECTRIFICATION ADMINISTRATION					
°Tri-State G&T #37	11/1	65,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #37	11/1	69,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #37	11/1	100,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #37	11/1	128,000.00	12/31/14	11.038%	10.890% qtr.
°Tri-State G&T #37	11/1	150,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #79	11/1	977,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #79	11/1	1,056,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #79	11/1	1,128,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	2,548,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	4,327,000.00	12/31/14	11.038%	10.890% qtr.
°Tri-State G&T #89	11/1	5,690,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	5,921,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	7,785,000.00	12/31/14	11.038%	10.890% qtr.
°Tri-State G&T #89	11/1	7,969,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	3,739,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #79	11/1	1,579,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	4,054,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #79	11/1	840,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	967,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	5,625,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	6,255,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #89	11/1	3,259,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #79	11/1	987,000.00	12/31/13	11.025%	10.877% qtr.

°early extension

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual	INTEREST RATE (other than semi-annual)
RURAL ELECTRIFICATION ADMINISTRATION (Cont'd)					
°Tri-State G&T #89	11/1	$ 6,485,000.00	12/31/13	11.025%	10.877% qtr.
°Tri-State G&T #37	11/1	300,000.00	12/31/13	11.025%	10.877% qtr.
Saluda River Electric #186	11/1	2,250,000.00	11/1/84	9.975%	9.854% qtr.
S. Mississippi Electric #171	11/1	2,769,000.00	11/2/84	9.975%	9.854% qtr.
Arkansas Electric #142	11/1	9,788,000.00	12/31/16	11.062%	10.913% qtr.
Arkansas Electric #221	11/1	1,231,000.00	12/31/16	11.062%	10.913% qtr.
Colorado Ute Electric #96	11/3	1,133,000.00	11/3/84	9.805%	9.688% qtr.
Tex-La Electric #208	11/3	760,000.00	11/3/84	9.805%	9.688% qtr.
Kansas Eletric #216	11/4	4,226,000.00	12/31/16	10.780%	10.639% qtr.
Plains Electric G&T #149	11/5	1,270,000.00	12/31/16	10.725%	10.585% qtr.
Plains Electric G&T #215	11/5	923,000.00	12/31/16	10.725%	10.585% qtr.
*Seminole Electric #141	11/5	2,032,000.00	12/31/14	10.705%	10.565% qtr.
*Southern Illinois Power #38	11/6	855,000.00	12/31/12	10.699%	10.560% qtr.
*San Miguel Electric #110	11/8	10,000,000.00	12/31/13	10.713%	10.564% qtr.
United Power #145	11/9	1,150,000.00	12/31/16	10.751%	10.610% qtr.
United Power #139	11/9	3,700,000.00	12/31/16	10.751%	10.610% qtr.
Cont. Tele. of Kansas #201	11/9	531,000.00	12/31/16	10.751%	10.610% qtr.
*Sierra Telephone #59	11/9	120,000.00	11/9/85	10.095%	9.971 qtr.
°Basin Electric #137	11/10	35,000,000.00	12/31/14	10.601%	10.464% qtr.
*Western Illinois Power #162	11/10	2,221,000.00	12/31/14	10.601%	10.464% qtr.
Hoosier Energy #107	11/10	15,000,000.00	11/10/84	9.865%	9.746% qtr.
Wolverine Electric #233	11/10	4,380,000.00	11/10/84	9.865%	9.746% qtr.
Wabash Valley Power #104	11/10	269,000.00	12/31/16	10.594%	10.457% qtr.
Allegheny Electric #175	11/10	4,160,000.00	12/31/16	10.594%	10.457% qtr.
New Hampshire Electric #192	11/10	565,000.00	12/31/16	10.594%	10.457% qtr.
East Kentucky Power #73	11/10	900,000.00	12/31/16	10.594%	10.457% qtr.
East Kentucky Power #140	11/10	600,000.00	12/31/16	10.594%	10.457% qtr.
East Kentucky Power #188	11/10	5,500,000.00	12/31/16	10.594%	10.457% qtr.
N. Michigan Electric #234	11/10	5,456,000.00	11/10/84	9.865%	9.746% qtr.
Deseret G&T #211	11/12	4,671,000.00	11/15/84	9.895%	9.776% qtr.
*Corn Belt Power #166	11/12	400,000.00	12/31/14	10.557%	10.421% qtr.
*Wolverine Electric #100	11/13	1,305,000.00	11/13/85	10.155%	10.029% qtr.
*Colorado Ute Electric #96	11/13	1,486,000.00	11/13/85	10.155%	10.029% qtr.
*N. Michigan Electric #101	11/13	2,543,000.00	11/13/84	9.995%	9.873% qtr.
*Deseret G&T #170	11/14	695,000.00	11/14/84	9.995%	9.873% qtr.
*Central Electric Power #131	11/14	120,000.00	11/14/84	9.995%	9.873% qtr.
Central Electric Power #131	11/15	500,000.00	11/15/84	9.995%	9.873% qtr.
New Hampshire Electric #192	11/15	985,000.00	12/31/16	10.606%	10.469% qtr.
*Oglethorpe Power #74	11/15	6,210,000.00	12/31/14	10.628%	10.490% qtr.
*Oglethorpe Power #150	11/15	7,057,000.00	12/31/14	10.628%	10.490% qtr.
New Hampshire Electric #192	11/15	7,760,000.00	12/31/16	10.606%	10.469% qtr.
*Soyland Power Coop. #165	11/17	8,562,000.00	11/17/84	10.025%	9.902% qtr.
*N. Michigan Electric #101	11/17	140,000.00	11/17/84	10.025%	9.902% qtr.
*Western Illinois Power #99	11/17	1,584,000.00	12/31/12	10.777%	10.636% qtr.
Seminole Electric #141	11/18	11,747,000.00	12/31/16	10.691%	10.552% qtr.
Oglethorpe Power #74	11/18	4,829,000.00	12/31/16	10.691%	10.552% qtr.
Seminole Electric #141	11/19	5,410,000.00	12/31/14	10.526%	10.391% qtr.
Tri-State G&T #157	11/19	1,440,000.00	12/31/16	10.513%	10.378% qtr.
*South Mississippi Electric #3	11/20	9,125,000.00	12/31/09	10.525%	10.390% qtr.
Big Rivers Electric #58	11/20	4,340,000.00	11/20/85	10.005%	9.883% qtr.
Big Rivers Electric #91	11/20	3,780,000.00	11/20/85	10.005%	9.883% qtr.
*Central Iowa Power #169	11/20	4,031,000.00	12/31/14	10.515%	10.380% qtr.
*East Kentucky Power #73	11/22	7,243,000.00	12/31/12	10.522%	10.387% qtr.
Big Rivers Electric #91	11/22	237,000.00	11/22/84	9.915%	9.795% qtr.
Big Rivers Electric #143	11/22	968,000.00	11/22/84	9.915%	9.795% qtr.
Big Rivers Electric #179	11/22	27,336,000.00	11/22/84	9.915%	9.795% qtr.
Western Illinois Power #225	11/23	2,688,000.00	12/31/16	10.557%	10.421% qtr.
Wabash Valley Power #206	11/23	192,000.00	12/31/16	10.557%	10.421% qtr.
Big Rivers Electric #179	11/24	5,500,000.00	11/24/84	9.855%	9.737% qtr.
*South Mississippi Electric #4	11/24	824,000.00	11/22/85	10.035%	9.912% qtr.
*South Mississippi Electric #90	11/24	1,321,000.00	11/22/85	10.035%	9.912% qtr.
°Big Rivers Electric #136	11/24	134,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #143	11/24	100,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #179	11/24	5,534,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #58	11/24	$ 1,825,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #91	11/24	1,551,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #136	11/24	1,161,000.00	12/31/13	10.628%	10.490% qtr.

°early extension
*maturity extension

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual	INTEREST RATE (other than semi-annual)
RURAL ELECTRIFICATION ADMINISTRATION (Cont'd)					
°Big Rivers Electric #58	11/24	$ 3,905,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #91	11/24	4,367,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #58	11/24	2,464,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #65	11/24	50,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #91	11/24	2,532,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #136	11/24	364,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #58	11/24	2,742,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #65	11/24	228,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #91	11/24	1,910,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #136	11/24	288,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #58	11/24	2,420,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #91	11/24	1,236,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #136	11/24	123,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #58	11/24	2,497,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #136	11/24	1,328,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #91	11/24	5,200,000.00	12/31/13	10.628%	10.490% qtr.
°Big Rivers Electric #91	11/24	1,004,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #136	11/24	519,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #143	11/24	22,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #179	11/24	6,377,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #91	11/24	345,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #136	11/24	357,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #143	11/24	35,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #179	11/24	6,794,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #91	11/24	392,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #136	11/24	182,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #143	11/24	45,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #179	11/24	12,192,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #91	11/24	328,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #179	11/24	2,874,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #179	11/24	16,248,000.00	12/31/15	10.624%	10.487% qtr.
°Big Rivers Electric #91	11/24	380,000.00	12/31/15	10.624%	10.487% qtr.
*Colorado Ute Electric #168	11/25	27,000,000.00	4/25/85	9.985%	9.863% qtr.
*Big Rivers Electric #58	11/25	170,000.00	11/25/84	9.925%	9.805% qtr.
*Big Rivers Electric #91	11/25	1,059,000.00	11/25/84	9.925%	9.805% qtr.
*Big Rivers Electric #136	11/25	123,000.00	11/25/84	9.925%	9.805% qtr.
*Big Rivers Electric #143	11/25	46,000.00	11/25/84	9.925%	9.805% qtr.
*Basin Electric #87	11/26	838,000.00	12/31/14	10.683%	10.544% qtr.
*Brazos Electric #108	11/26	632,000.00	12/31/14	10.683%	10.544% qtr.
*Brazos Electric #144	11/26	820,000.00	12/31/14	10.683%	10.544% qtr.
*South Texas Electric #109	11/28	527,000.00	11/28/84	9.885%	9.766% qtr.
North Carolina Electric #185	11/29	4,755,000.00	11/29/84	9.885%	9.766% qtr.
Chugach Electric #204	11/29	750,000.00	12/31/16	10.610%	10.473% qtr.
Associated Electric #132	11/29	9,195,000.00	12/31/16	10.610%	10.473% qtr.
Western Farmers Electric #220	11/29	5,225,000.00	12/31/16	10.610%	10.473% qtr.
Western Farmers Electric #133	11/29	460,000.00	12/31/16	10.610%	10.473% qtr.
°Associated Electric #132	11/29	300,000.00	12/31/13	10.616%	10.479% qtr.
°Associated Electric #132	11/29	10,500,000.00	12/31/13	10.616%	10.479% qtr.
°Associated Electric #132	11/29	8,000,000.00	12/31/13	10.616%	10.479% qtr.
°Associated Electric #132	11/29	17,300,000.00	12/31/13	10.616%	10.479% qtr.
°Associated Electric #132	11/29	10,500,000.00	12/31/13	10.616%	10.479% qtr.
°Associated Electric #132	11/29	13,850,000.00	12/31/13	10.616%	10.479% qtr.
°Associated Electric #132	11/29	2,750,000.00	12/31/15	10.612%	10.475% qtr.
°Associated Electric #132	11/29	10,000,000.00	12/31/15	10.612%	10.475% qtr.
°Associated Electric #132	11/29	12,100,000.00	12/31/15	10.612%	10.475% qtr.
°Associated Electric #132	11/29	4,100,000.00	12/31/15	10.612%	10.475% qtr.
°Associated Electric #132	11/29	12,000,000.00	12/31/15	10.612%	10.475% qtr.
Colorado Ute Electric #168	11/30	12,660,000.00	3/31/85	9.955%	9.834% qtr.
Tex-La Electric #208	11/30	800,000.00	11/30/84	10.065%	9.941% qtr.
Seminole Electric #141	11/30	3,542,000.00	12/31/16	10.875%	10.731% qtr.
Plains Electric G&T #158	11/30	13,157,000.00	12/31/16	10.875%	10.731% qtr.
*Allegheny Electric #93	11/30	2,638,000.00	12/31/14	10.878%	10.734% qtr.
*Southern Illinois Power #38	11/30	3,415,000.00	12/31/11	10.881%	10.737% qtr.
*Southern Illinois Power #38	11/30	1,100,000.00	12/31/13	10.879%	10.735% qtr.

*maturity extension
°early extension

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual	INTEREST RATE (other than semi-annual)
SMALL BUSINESS ADMINISTRATION					
State & Local Development Company Debentures					
San Diego County LDC	11/10	$ 53,000.00	11/1/97	10.663%	
Iowa Business Growth Company	11/10	54,000.00	11/1/97	10.663%	
Atlanta LDC	11/10	59,000.00	11/1/97	10.663%	
San Diego County LDC	11/10	69,000.00	11/1/97	10.663%	
Caprock LDC	11/10	82,000.00	11/1/97	10.663%	
Scioto EDC	11/10	98,000.00	11/1/97	10.663%	
Maine Development Foundation	11/10	126,000.00	11/1/97	10.663%	
Grand Rapids LDC	11/10	164,000.00	11/1/97	10.663%	
Old Colorado City Dev. Co.	11/10	175,000.00	11/1/97	10.663%	
Grand Rapids LDC	11/10	196,000.00	11/1/97	10.663%	
Commonwealth SBDC	11/10	210,000.00	11/1/97	10.663%	
Metro. Growth & Dev. Corp.	11/10	280,000.00	11/1/97	10.663%	
Greater Spokane BDA	11/10	52,000.00	11/1/02	10.176%	
Bedco Development Corporation	11/10	56,000.00	11/1/02	10.176%	
Androscoggin Valley RPC	11/10	60,000.00	11/1/02	10.176%	
Texas Certified Dev. Co. Inc.	11/10	67,000.00	11/1/02	10.176%	
Evergreen Community DCA	11/10	67,000.00	11/1/02	10.176%	
Greater Kenosha Dev. Corp.	11/10	70,000.00	11/1/02	10.176%	
Texas Certified DCI	11/10	70,000.00	11/1/02	10.176%	
Greater Kenosha Dev. Corp.	11/10	83,000.00	11/1/02	10.176%	
South Shore EDC	11/10	97,000.00	11/1/02	10.176%	
St. Louis LDC	11/10	103,000.00	11/1/02	10.176%	
San Diego County LDC	11/10	118,000.00	11/1/02	10.176%	
City-Wide SBDC	11/10	132,000.00	11/1/02	10.176%	
Milwaukee Economic Dev. Corp.	11/10	168,000.00	11/1/02	10.176%	
Long Beach LDC	11/10	370,000.00	11/1/02	10.176%	
St. Paul 503 Dev. Co.	11/10	47,000.00	11/1/07	10.745%	
Tuscon LDC	11/10	57,000.00	11/1/07	10.745%	
St. Louis LDC	11/10	67,000.00	11/1/07	10.745%	
Columbus Countywide Dev. Corp.	11/10	84,000.00	11/1/07	10.745%	
Ocean State BDA Inc.	11/10	92,000.00	11/1/07	10.745%	
Columbus Countywide Dev. Corp.	11/10	105,000.00	11/1/07	10.745%	
St. Paul 503 Dev. Co.	11/10	123,000.00	11/1/07	10.745%	
McPherson County SBA	11/10	129,000.00	11/1/07	10.745%	
San Diego County LDC	11/10	134,000.00	11/1/07	10.745%	
Milwaukee Economic Dev. Corp.	11/10	195,000.00	11/1/07	10.745%	
Bay Colony Development Corp.	11/10	200,000.00	11/1/07	10.745%	
Hazen Community Dev. Inc.	11/10	220,000.00	11/1/07	10.745%	
Columbus Countywide Dev. Corp.	11/10	252,000.00	11/1/07	10.745%	
Bedco Development Corporation	11/10	282,000.00	11/1/07	10.745%	
Bay Area Employment Dev. Co.	11/10	364,000.00	11/1/07	10.745%	
Bay Area Employment Dev. Co.	11/10	500,000.00	11/1/07	10.745%	
Small Business Investment Company Debentures					
Texas Capital Corp.	11/24	500,000.00	11/1/87	10.375%	
Crosspoint Investment Corp.	11/24	300,000.00	11/1/89	10.565%	
Brentwood Capital Corp.	11/24	4,000,000.00	11/1/92	10.555%	
J&D Capital Corp.	11/24	500,000.00	11/1/92	10.555%	
Noro Capital Corp.	11/24	500,000.00	11/1/92	10.555%	
Rust Capital LTD	11/24	1,500,000.00	11/1/92	10.555%	
Seafirst Capital Corp.	11/24	1,000,000.00	11/1/92	10.555%	
South Texas SBI Co.	11/24	1,000,000.00	11/1/92	10.555%	
TLC Funding Corp.	11/24	500,000.00	11/1/92	10.555%	
Texas Capital Corp.	11/24	1,500,000.00	11/1/92	10.555%	
Universal Investment Corp.	11/24	400,000.00	11/1/92	10.555%	
TENNESSEE VALLEY AUTHORITY					
Seven States Energy Corporation					
Note A-83-2	11/30	482,236,194.07	2/28/83	8.480%	
DEPARTMENT OF TRANSPORTATION					
Section 511					
Milwaukee Road 511-2	11/22	649,115.00	6/30/06	10.541%	

FEDERAL FINANCING BANK
November 1982 Commitments

BORROWER	AMOUNT	GUARANTOR	COMMITMENT EXPIRES	MATURITY
Beaumont, TX	$ 1,050,000.00	HUD	9/1/83	9/1/83
Lynn, MA	10,500,000.00	HUD	8/15/84	8/15/93
Schenectady, NY	1,500,000.00	HUD	8/15/84	8/15/84
St. Paul, MN	5,000,000.00	HUD	8/1/83	8/1/03
Baltimore, MD	2,000,000.00	HUD	1/2/84	1/2/04
Gary, IN	967,000.00	HUD	9/1/83	9/1/83
Nashville/Davidson County, TN	2,500,000.00	HUD	6/1/84	6/1/84
Baldwin Park, CA	800,000.00	HUD	8/15/84	8/15/91
Gulfport, MS	235,000.00	HUD	6/15/84	6/15/84
Des Moines, IO	750,000.00	HUD	2/15/84	2/15/84

FEDERAL FINANCING BANK HOLDINGS
(in millions)

Program	October 31, 1982	November 30, 1982	Net Change 11/1/82-11/30/82	Net Change 10/1/82-11/30/82
On-Budget Agency Debt				
Tennessee Valley Authority	$ 12,460.0	$ 12,545.0	$ 85.0	$ 260.0
Export-Import Bank	13,953.9	13,953.9	-0-	-0-
NCUA-Central Liquidity Facility	145.0	135.3	-9.8	5.2
Off-Budget Agency Debt				
U.S. Postal Service	1,221.0	1,221.0	-0-	-0-
U.S. Railway Association	191.5	191.5	-0-	-3.4
Agency Assets				
Farmers Home Administration	53,661.0	53,661.0	-0-	-75.0
DHHS-Health Maintenance Org.	131.0	114.3	-16.8	-16.8
DHHS-Medical Facilities	145.7	148.8	3.0	3.0
Overseas Private Investment Corp	21.5	21.5	-0-	-0-
Rural Electrification Admin.-CBO	3,123.7	3,123.7	-0-	-0-
Small Business Administration	57.3	56.7	-.6	-1.4
Government-Guaranteed Loans				
DOD-Foreign Military Sales	11,630.7	11,990.5	359.8	554.7
DEd.-Student Loan Marketing Assn.	5,000.0	5,000.0	-0-	-0-
DOE-Geothermal Loans	40.9	40.9	-0-	4.3
DOE-Non-Nuclear Act (Great Plains)	378.5	426.0	47.5	86.0
DHUD-Community Dev. Block Grant	119.0	115.6	-3.4	-1.4
DHUD-New Communities	33.5	33.5	-0-	-0-
DHUD-Public Housing Notes	1,659.0	1,652.8	-6.2	28.5
General Services Administration	420.5	420.1	-.4	-.4
DOI-Guam Power Authority	36.0	36.0	-0-	-0-
DOI-Virgin Islands	29.5	29.5	-0-	-0-
NASA-Space Communications Co.	774.3	782.4	8.1	24.6
Rural Electrification Admin.	16,600.0	16,750.2	150.2	468.7
SBA-Small Business Investment Cos.	721.0	731.6	10.7	19.6
SBA-State/Local Development Cos.	53.7	59.6	5.9	11.2
TVA-Seven States Energy Corp.	1,233.6	1,246.1	12.5	-11.8
DOT-Amtrak	855.4	855.4	-0-	-0-
DOT-Section 511	190.0	187.1	-2.7	-5.9
DOT-WMATA	177.0	177.0	-0-	-0-
TOTALS*	$ 125,064.2	$ 125,707.0	$ 642.8	$ 1,349.8

*figures may not total due to rounding

DECEMBER 1982 ACTIVITY

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
ON-BUDGET AGENCY DEBT					
TENNESSEE VALLEY AUTHORITY					
Note #272	12/10	$ 20,000,000.00	3/3/83	8.404%	
Note #275	12/31	75,000,000.00	3/3/83	8.435%	
EXPORT-IMPORT BANK					
Note #45	12/1	369,000,000.00	12/1/92	10.915%	10.770% qtr.
Note #46	12/1	223,000,000.00	12/1/92	10.638%	10.500% qtr.
NATIONAL CREDIT UNION ADMINISTRATION					
Central Liquidity Facility					
Note #141	12/1	3,000,000.00	3/1/83	8.668%	
Note #142	12/3	500,000.00	12/17/82	8.423%	
Note #143	12/14	14,987,000.00	3/14/83	8.398%	
Note #144	12/15	2,000,000.00	3/1/83	8.034%	
Note #145	12/16	1,500,000.00	12/30/82	7.981%	
Note #146	12/16	13,000,000.00	2/14/83	7.981%	
Note #147	12/17	500,000.00	12/29/82	8.191%	
Note #148	12/20	13,500,000.00	3/21/83	8.227%	
OFF-BUDGET AGENCY DEBT					
UNITED STATES RAILWAY ASSOCIATION					
Note #33	12/27	4,623,063.54	12/26/90	10.585%	
AGENCY ASSETS					
DEPARTMENT OF HEALTH & HUMAN SERVICES					
Health Maintenance Organization Notes					
Block #26	12/15	2,476,919.06	7/1/02-7/11/04	10.596%	
GOVERNMENT - GUARANTEED LOANS					
DEPARTMENT OF DEFENSE - FOREIGN MILITARY SALES					
Egypt 3	12/1	3,774,529.47	6/15/12	10.896%	
Greece 13	12/1	100,800.00	9/22/90	10.505%	
Indonesia 7	12/1	1,813,000.00	3/20/90	10.461%	
Indonesia 8	12/1	2,205,023.00	5/5/91	10.574%	
Jamaica 2	12/1	41,482.00	12/20/93	10.788%	
Jordan 7	12/1	1,192,267.21	3/16/90	10.461%	
Korea 15	12/1	250,000.00	12/31/93	10.724%	
Morocco 9	12/1	5,086,938.77	3/31/94	10.738%	
Spain 4	12/1	40,299.19	4/25/90	10.464%	
Ecuador 6	12/3	$ 471,845.00	6/20/89	10.354%	
Israel 8	12/3	1,186,118.00	9/1/09	10.796%	
Israel 13	12/3	5,164,324.58	2/16/12	10.796%	
Spain 5	12/3	912,248.42	6/15/91	10.475%	
Turkey 11	12/3	1,806,518.00	12/22/10	10.799%	
Turkey 13	12/3	2,514,200.00	3/24/12	10.797%	
Egypt 3	12/6	5,341,596.48	6/15/12	10.586%	
Israel 8	12/6	250,000.00	9/1/09	10.586%	
Thailand 10	12/6	1,636,000.00	7/10/94	10.524%	
Columbia 4	12/7	42,311.30	7/10/86	9.831%	
Egypt 3	12/8	23,767,733.37	6/15/12	10.595%	
Greece 14	12/8	348,828.48	4/30/11	10.596%	
Honduras 9	12/8	719,910.38	9/20/94	10.556%	
Israel 13	12/8	11,947,231.17	2/16/12	10.595%	
Tunisia 11	12/8	452,312.00	5/5/92	10.433%	
Turkey 11	12/8	459,039.64	12/22/10	10.596%	

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
DEPARTMENT OF DEFENSE - FOREIGN MILITARY SALES (Cont'd)					
Korea 15	12/9	$ 716,589.00	12/31/93	10.571%	
Israel 8	12/9	582,198.76	9/1/09	10.733%	
Israel 13	12/9	9,854,993.24	2/16/12	10.730%	
Columbia 4	12/9	68,502.00	7/10/86	9.941%	
Egypt 3	12/10	345,220.14	6/15/12	10.695%	
Indonesia 8	12/10	7,025,865.00	5/5/91	10.458%	
Jordan 7	12/10	1,620,837.11	3/16/90	10.345%	
Philippines 7	12/10	198,609.23	9/10/87	10.095%	
Turkey 9	12/14	322,694.00	6/22/92	10.577%	
Jordan 7	12/15	5,034,417.40	3/16/90	10.149%	
Oman 5	12/15	2,916,601.74	5/25/90	10.170%	
Thailand 6	12/15	1,361,993.00	9/20/85	9.476%	
Thailand 7	12/15	102,214.28	8/25/86	9.670%	
Thailand 8	12/15	1,109,847.00	8/10/90	10.296%	
Thailand 9	12/15	19,836,078.00	9/15/93	10.472%	
Israel 8	12/15	3,710,000.00	9/1/09	10.582%	
Honduras 9	12/16	1,029,550.00	9/20/94	10.564%	
Indonesia 8	12/16	1,151,452.00	5/5/91	10.310%	
Israel 13	12/17	10,557,739.28	2/16/12	10.731%	
Egypt 3	12/21	199,135,979.94	6/15/12	10.834%	
El Salvador 4	12/21	85,556.00	12/5/93	10.727%	
Israel 8	12/21	2,000,000.00	9/1/09	10.827%	
Jamaica 2	12/21	47,267.29	12/20/93	10.731%	
Tunisia 11	12/21	41,057,779.53	5/5/92	10.619%	
Turkey 9	12/23	2,089,715.33	6/22/92	10.492%	
Dominican Republic 5	12/23	3,509.42	4/30/89	10.170%	
Honduras 9	12/23	224,614.54	9/20/94	10.612%	
Peru 7	12/23	1,398.00	2/15/88	10.025%	
Philippines 7	12/23	904,140.72	9/10/87	9.958%	
Turkey 13	12/23	971,589.25	3/24/12	10.746%	
Honduras 9	12/27	1,504,834.37	9/20/94	10.540%	
Korea 15	12/27	1,463,635.97	12/31/93	10.443%	
Philippines 7	12/27	836,025.00	9/10/87	9.900%	
Egypt 3	12/29	1,999,792.96	6/15/12	10.655%	
Greece 14	12/29	1,330,983.96	4/30/11	10.656%	
Honduras 9	12/29	222,181.00	9/20/94	10.510%	
Egypt 3	12/30	3,217,526.28	6/15/12	10.697%	
Greece 14	12/30	171,941.91	4/30/11	10.696%	
Israel 8	12/30	669,345.00	9/1/09	10.693%	
Jordan 8	12/30	1,876,421.89	11/22/90	10.282%	
Peru 7	12/30	300,000.00	2/15/88	9.987%	
Spain 6	12/30	8,090,000.00	9/15/92	10.404%	
Thailand 9	12/30	2,865,612.00	9/15/93	10.505%	
DEPARTMENT OF ENERGY					
Synthetic Fuels Guarantees - Non-Nuclear Act					
Great Plains Gasification Assoc. #40	12/1	10,500,000.00	7/1/02	11.624%	
#41	12/6	7,000,000.00	7/1/02	11.525%	
#42	12/13	15,500,000.00	4/1/83	9.305%	
#43	12/20	9,000,000.00	4/1/83	9.015%	
#44	12/27	8,500,000.00	7/1/83	9.345%	
DEPARTMENT OF HOUSING & URBAN DEVELOPMENT					
Community Development Block Grant Guarantees					
Baltimore, MD	12/1	250,000.00	1/2/04	10.888%	11.184% ann.
Kenosha, WI	12/1	14,000.00	6/1/83	9.185%	
Phil. Auth. for Ind. Dev.	12/1	850,000.00	10/1/03	10.887%	11.183% ann.
Washington County, PA	12/1	139,580.95	8/1/83	9.295%	9.406% ann.
Washington County, PA	12/7	53,613.18	8/1/83	8.935%	9.029% ann.
Hammond, IN	12/7	115,530.00	5/1/84	9.525%	9.752% ann.
Phila. Housing Dev. Auth	12/8	3,509,742.00	8/15/90	10.405%	10.676% ann.
Gary, IN	12/10	345,000.00	9/1/83	9.015%	9.140% ann.
Rochester, NY	12/14	334,000.00	8/31/02	10.701%	10.987% ann.
Des Moines, Iowa	12/15	230,000.00	2/15/84	9.005%	9.208% ann.
Gary, IN	12/15	142,000.00	9/1/83	8.565%	8.673% ann.

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
Community Development Block Grant Guarantees (Cont'd)					
Washington, PA	12/15	$ 29,024.62	8/1/83	8.505%	8.580% ann.
Baltimore, MD	12/20	205,000.00	1/2/04	10.740%	11.028% ann.
Kenosha, WI	12/20	24,100.00	6/1/83	8.615%	
Lawrence, Mass.	12/20	23,400.00	1/1/83	8.227%	
Tacoma, WA	12/20	1,000,000.00	10/15/03	10.739%	11.027% ann.
Niagera Falls Urban Renewal Ag	12/22	575,000.00	7/1/04	10.722%	11.009% ann.
Hammond, IN	12/30	460,389.00	5/1/84	9.025%	9.417% ann.
Kenosha, WI	12/30	57,463.46	6/1/83	8.665%	
Long Beach, CA	12/30	1,824,632.00	2/1/85	9.436%	9.659% ann.
Public Housing Notes					
Sale #28	12/10	22,872,250.12	11/1/02-11/1/19	10.696%	10.982% ann.
NATIONAL AERONAUTICS AND SPACE ADMINISTRATION					
Space Communications Company	12/1	17,000,000.00	10/1/92	10.709%	10.996% ann.
	12/20	14,900,000.00	10/1/92	10.553%	10.831% ann.
RURAL ELECTRIFICATION ADMINISTRATION					
Brazos Electric #108	12/1	958,000.00	12/1/84	10.085%	9.961% qtr.
Brazos Electric #230	12/1	5,795,000.00	12/1/84	10.085%	9.961% qtr.
S. Mississippi Electric #90	12/1	150,000.00	12/2/84	10.085%	9.961% qtr.
S. Mississippi Electric #171	12/1	4,688,000.00	12/2/84	10.085%	9.961% qtr.
Saluda River Electric #186	12/1	1,500,000.00	12/31/16	10.863%	10.719% qtr.
North Florida Tele. #186	12/1	4,569,000.00	12/31/16	10.863%	10.719% qtr.
Arkansas Electric #221	12/1	106,000.00	12/31/16	10.863%	10.719% qtr.
Arkansas Electric #142	12/1	18,329,000.00	12/31/16	10.863%	10.719% qtr.
*Big Rivers Electric #91	12/1	600,000.00	12/1/84	10.085%	9.961% qtr.
*Arkansas Electric #142	12/1	13,824,000.00	12/31/14	10.895%	10.751% qtr.
*S. Mississippi Electric #171	12/2	65,000,000.00	12/31/14	10.841%	10.698% qtr.
Sugar Land Telephone Co. #69	12/3	1,771,000.00	12/3/84	10.015%	9.893% qtr.
*Southern Illinois Power #38	12/4	500,000.00	12/31/12	10.581%	10.445% qtr.
Central Electric Power #131	12/6	550,000.00	12/6/84	9.845%	9.727% qtr.
*Eastern Iowa L&T #61	12/6	1,400,000.00	12/31/12	10.581%	10.445% qtr.
°United Power #86	12/8	3,191,000.00	12/31/15	10.592%	10.455% qtr.
°United Power #139	12/8	3,755,000.00	12/31/15	10.592%	10.455% qtr.
Sho-me Power #164	12/9	1,300,000.00	12/31/16	10.705%	10.565% qtr.
Dairyland Power #54	12/9	699,000.00	12/9/84	9.975%	9.854% qtr.
Wolverine Electric #233	12/10	3,852,000.00	12/10/84	9.955%	9.834% qtr.
Wabash Valley Power #104	12/10	6,991,000.00	12/10/84	9.955%	9.834% qtr.
Wabash Valley Power #206	12/10	230,000.00	12/10/84	9.955%	9.834% qtr.
Allegheny Electric #175	12/10	3,366,000.00	12/31/84	9.965%	9.844% qtr.
Deseret G&T #211	12/10	27,315,000.00	12/31/16	10.674%	10.535% qtr.
N. Michigan Electric #234	12/10	4,899,000.00	12/10/84	9.955%	9.834% qtr.
*Wabash Valley Power #104	12/10	3,190,000.00	12/31/14	10.679%	10.540% qtr.
*East River Electric #117	12/10	2,000,000.00	12/10/84	9.955%	9.834% qtr.
*N. Michigan Electric #101	12/10	1,338,000.00	12/10/84	9.955%	9.834% qtr.
*Colorado Ute Electric #96	12/11	1,540,000.00	12/11/84	9.995%	9.873% qtr.
*Alabama Electric #26	12/11	9,900,000.00	12/31/12	10.773%	10.632% qtr.
*Wolverine Electric #100	12/11	1,020,000.00	12/11/84	9.995%	9.873% qtr.
*Sunflower Electric #63	12/12	1 650,000.00	12/31/14	10.773%	10.632% qtr.
East Kentucky Power #140	12/13	1,400,000.00	12/31/16	10.773%	10.632% qtr.
East Kentucky Power #188	12/13	6,900,000.00	12/31/16	10.773%	10.632% qtr.
*Northwest Iowa Power #95	12/14	4,048,000.00	12/14/84	9.965%	9.844% qtr.
Colorado Ute Electric #203	12/14	993,000.00	12/14/85	10.125%	10.000% qtr.
*Deseret G&T #170	12/15	1,420,000.00	12/31/14	10.599%	10.462% qtr.
*Cajun Electric #147	12/15	33,000,000.00	12/31/14	10.599%	10.462% qtr.
*East Kentucky Power #140	12/15	500,000.00	12/31/14	10.599%	10.462% qtr.
Colorado Ute Electric #96	12/15	3,176,000.00	12/15/84	9.665%	9.551% qtt.
New Hampshire Electric #192	12/15	1,805,000.00	12/15/84	9.665%	9.551% qtr.
*Western Illinois Power #99	12/15	1,428,000.00	12/31/12	10.593%	10.456% qtr.
*Oglethorpe Electric Corp. #150	12/15	10,786,000.00	12/31/14	10.597%	10.460% qtr.
*Oglethorpe Electric Corp. #74	12/15	6,156,000.00	12/31/14	10.597%	10.460% qtr.
*Dairyland Power #173	12/15	10,000,000.00	12/15/84	9.665%	9.551% qtr.

°early extension
*maturity extension

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
RURAL ELECTRIFICATION ADMINISTRATION (Cont'd)					
Colorado Ute Electric #203	12/16	$ 7,229,000.00	12/16/84	9.715%	9.600% qtr.
Mid-Georgia Telephone #229	12/16	2,036,000.00	12/31/16	10.655%	10.517% qtr.
*San Miguel Electric Coop. #110	12/16	3,400,000.00	12/31/14	10.651%	10.513% qtr.
Northwest Iowa Power #95	12/17	2,252,000.00	12/17/84	9.715%	9.600% qtr.
Upper Missouri G&T #172	12/17	192,000.00	12/17/84	9.715%	9.600% qtr.
Eastern Iowa L&P #184	12/17	1,994,000.00	12/31/16	10.766%	10.625% qtr.
United Power Assoc. #145	12/17	875,000.00	12/31/16	10.766%	10.625% qtr.
United Power Assoc. #139	12/17	4,100,000.00	12/31/16	10.766%	10.625% qtr.
°Sierra Telephone #59	12/17	281,904.00	12/31/11	10.631%	10.493% qtr.
°Sierra Telephone #59	12/17	48,000.00	12/31/11	10.631%	10.493% qtr.
°Sierra Telephone #59	12/17	300,000.00	12/31/11	10.631%	10.493% qtr.
°Sierra Telephone #59	12/17	1,271,000.00	12/31/11	10.631%	10.493% qtr.
°Sierra Telephone #59	12/17	232,826.00	12/31/11	10.632%	10.494% qtr.
°Sierra Telephone #59	12/17	273,013.00	12/31/11	10.632%	10.494% qtr.
°Sierra Telephone #59	12/17	248,000.00	12/31/11	10.632%	10.494% qtr.
°Sierra Telephone #59	12/17	492,000.00	12/31/12	10.638%	10.500% qtr.
°Sierra Telephone #59	12/17	220,000.00	12/31/12	10.638%	10.500% qtr.
°Sierra Telephone #59	12/17	108,160.00	12/31/12	10.638%	10.500% qtr.
°Sierra Telephone #59	12/17	148,645.00	12/31/12	10.638%	10.500% qtr.
°Sierra Telephone #59	12/17	74,000.00	12/31/12	10.638%	10.500% qtr.
°Sierra Telephone #59	12/17	120,000.00	12/31/12	10.638%	10.500% qtr.
°Sierra Telephone #59	12/17	265,000.00	12/31/13	10.645%	10.507% qtr.
°Sierra Telephone #59	12/17	121,000.00	12/31/13	10.645%	10.507% qtr.
°Sierra Telephone #59	12/17	92,000.00	12/31/14	10.650%	10.512% qtr.
°Sierra Telephone #59	12/17	76,000.00	12/31/14	10.650%	10.512% qtr.
°Sierra Telephone #59	12/17	207,000.00	12/31/15	10.655%	10.517% qtr.
°Sierra Telephone #59	12/17	15,000.00	12/31/16	10.658%	10.520% qtr.
*Seminole Electric Coop. #141	12/17	4,424,000.00	12/31/14	10.758%	10.617% qtr.
Western Illinois Power #162	12/17	2,315,000.00	12/31/14	10.758%	10.617% qtr.
Colorado Ute Electric #168	12/18	8,014,000.00	1/18/85	9.815%	9.697% qtr.
*St. Joseph T&T #13	12/20	439,000.00	12/20/84	9.785%	9.668% qtr.
*Big Rivers Electric #58	12/20	3,033,000.00	12/31/12	10.773%	10.632% qtr.
Big Rivers Electric #65	12/20	104,000.00	12/31/12	10.773%	10.632% qtr.
*Big Rivers Electric #91	12/20	3,840,000.00	12/31/12	10.773%	10.632% qtr.
Soyland Power #226	12/20	13,800,000.00	12/20/84	9.785%	9.668% qtr.
Basin Electric #232	12/20	9,512,000.00	12/20/84	9.785%	9.668% qtr.
*San Miguel Electric #110	12/20	10,000,000.00	12/31/12	10.769%	10.628% qtr.
Big Rivers Electric #91	12/21	4,713,000.00	12/31/16	10.864%	10.720% qtr.
Big Rivers Electric #143	12/21	1,815,000.00	12/31/16	10.864%	10.720% qtr.
Big Rivers Electric #179	12/21	3,513,000.00	12/31/16	10.864%	10.720% qtr.
Seminole Electric Coop. #141	12/21	22,639,000.00	12/31/16	10.864%	10.720% qtr.
Wabash Valley Power #252	12/22	37,015,000.00	12/22/84	9.675%	9.561% qtr.
Wabash Valley Power #252	12/22	2,000,000.00	6/22/85	9.845%	9.727% qtr.
Wabash Valley Power #252	12/22	350,000.00	12/22/85	10.005%	9.883% qtr.
Wabash Valley Power #252	12/22	2,000,000.00	6/22/86	10.135%	10.010% qtr.
Wabash Valley Power #252	12/22	400,000.00	12/22/86	10.235%	10.107% qtr.
Wabash Valley Power #252	12/22	2,000,000.00	6/22/87	10.285%	10.156% qtr.
Wabash Valley Power #252	12/22	450,000.00	12/22/87	10.335%	10.205% qtr.
Wabash Valley Power #252	12/22	2,000,000.00	6/22/88	10.425%	10.293% qtr.
Wabash Valley Power #252	12/22	500,000.00	12/22/88	10.515%	10.380% qtr.
Wabash Valley Power #252	12/22	30,000,000.00	12/31/16	10.706%	10.566% qtr.
Oglethorpe Power Corp. #74	12/22	26,521,000.00	12/31/16	10.706%	10.566% qtr.
*Big Rivers Electric #58	12/22	82,000.00	12/31/14	10.714%	10.574% qtr.
*Big Rivers Electric #91	12/22	1,865,000.00	12/31/14	10.714%	10.574% qtr.
*Big Rivers Electric #136	12/22	405,000.00	12/31/14	10.714%	10.574% qtr.
*Big Rivers Electric #143	12/22	22,000.00	12/31/14	10.714%	10.574% qtr.
*Colorado Ute Electric #71	12/23	1,720,000.00	2/23/85	9.735%	9.619% qtr.
*Brazos Electric #108	12/24	1,287,000.00	12/31/14	10.691%	10.552% qtr.
*Brazos Electric #144	12/24	3,523,000.00	12/31/14	10.691%	10.552% qtr.
Soyland Power #105	12/26	7,248,000.00	12/26/85	9.935%	9.815% qtr.
Kamo Electric #209	12/27	1,943,000.00	12/31/16	10.682%	10.543% qtr.
*East Kentucky Power #73	12/27	5,040,000.00	12/31/12	10.702%	10.563% qtr.
Wabash Valley Power #206	12/28	111,000.00	12/28/84	9.665%	9.551% qtr.
*East Ascension Tele. #39	12/28	500,000.00	12/31/12	10.652%	10.514% qtr.
Wolverine Electric #233	12/29	13,834,000.00	12/29/84	9.655%	9.541% qtr.
N. Michigan Electric #234	12/29	17,482,000.00	12/29/84	9.655%	9.541% qtr.
N. Carolina Electric #185	12/29	29,785,000.00	12/29/84	9.655%	9.541% qtr.

°early extension
*maturity extension

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual	INTEREST RATE (other than semi-annual)
RURAL ELECTRIFICATION ADMINISTRATION (Cont'd)					
Plains Electric G&T #158	12/29	$ 3,998,000.00	12/31/16	10.622%	10.485% qtr.
*Wolverine Electric #100	12/29	1,516,000.00	12/29/84	9.655%	9.541% qtr.
*Southern Illinois Power #38	12/29	650,000.00	12/13/12	10.647%	10.509% qtr.
Wabash Valley Power #104	12/30	9,328,000.00	12/30/84	9.665%	9.551% qtr.
Wabash Valley Power #206	12/30	432,000.00	12/30/84	9.665%	9.551% qtr.
New Hampshire Electric #192	12/30	1,280,000.00	12/30/84	9.665%	9.551% qtr.
Basin Electric #232	12/30	2,692,000.00	12/30/84	9.665%	9.551% qtr.
Tex-La Electric #208	12/30	3,436,000.00	12/30/84	9.665%	9.551% qtr.
Allegheny Electric #175	12/30	7,042,000.00	1/31/85	9.695%	9.580% qtr.
Associated Electric #132	12/30	16,475,000.00	12/31/16	10.674%	10.535% qtr.
Sunflower Electric #174	12/30	18,750,000.00	12/31/16	10.674%	10.535% qtr.
Big Rivers Electric #58	12/30	2,010,000.00	12/31/16	10.674%	10.535% qtr.
Big Rivers Electric #179	12/30	3,340,000.00	12/31/16	10.674%	10.535% qtr.
Saluda River Electric #186	12/30	10,569,000.00	12/31/16	10.674%	10.535% qtr.
*Southern Illinois Power #38	12/31	2,960,000.00	12/31/11	10.685%	10.546% qtr.
*Allegheny Electric #93	12/31	3,114,000.00	12/31/14	10.664%	10.526% qtr.
*Basin Electric #87	12/31	2,846,000.00	12/31/14	10.664%	10.526% qtr.
*Wabash Valley Power	12/31	3,920,000.00	12/31/14	10.664%	10.526% qtr.
*South Mississippi Power #3	12/31	504,000.00	12/31/12	10.678%	10.539% qtr.
*South Mississippi Power #90	12/31	246,000.00	12/31/12	10.678%	10.539% qtr.
*Wolverine Electric #182	12/31	14,946,000.00	12/31/84	9.645%	9.531% qtr.
*Wolverine Electric #100	12/31	1,997,000.00	12/31/84	9.645%	9.531% qtr.
*Big Rivers Electric #91	12/31	3,024,000.00	12/31/14	10.664%	10.526% qtr.
N. Michigan Electric #183	12/31	21,772,000.00	12/31/84	9.645%	9.531% qtr.
N. Michigan Electric #101	12/31	2,446,000.00	12/31/84	9.645%	9.531% qtr.
*Tri-State G&T #89	12/31	6,075,000.00	12/31/12	10.678%	10.539% qtr.
*Tri-State G&T #37	12/31	300,000.00	12/31/12	10.678%	10.539% qtr.
*Tri-State G&T #89	12/31	9,135,000.00	12/31/12	10.678%	10.539% qtr.
*Tri-State G&T #89	12/31	9,308,000.00	12/31/12	10.678%	10.539% qtr.
*Tri-State G&T #37	12/31	90,000.00	12/31/12	10.678%	10.539% qtr.
*Tri-State G&T #79	12/31	1,937,000.00	12/31/12	10.678%	10.539% qtr.
SMALL BUSINESS ADMINISTRATION					
Small Business Investment Company Debentures					
Edwards Capital Company	12/22	600,000.00	12/1/85	10.095%	
National City Capital Corp.	12/22	1,000,000.00	12/1/87	10.425%	
New West Partners	12/22	600,000.00	12/1/87	10.425%	
Frontenac Capital Corp.	12/22	1,000,000.00	12/1/89	10.815%	
Miami Valley Capital, Inc.	12/22	500,000.00	12/1/89	10.815%	
Rice Investment Company	12/22	600,000.00	12/1/89	10.815%	
Bando-McGlocklin Inv. Co.	12/22	1,500,000.00	12/1/92	10.825%	
Charleston Capital Corp.	12/22	500,000.00	12/1/92	10.825%	
Clinton Capital Corp.	12/22	900,000.00	12/1/92	10.825%	
Delta Capital, Inc.	12/22	850,000.00	12/1/92	10.825%	
First North Flordia SBIC	12/22	500,000.00	12/1/92	10.825%	
Nelson Capital Corp.	12/22	330,000.00	12/1/92	10.825%	
State & Local Development Company Debentures					
St. Louis Local Dev. Co.	12/8	16,000.00	12/1/97	10.528%	
Metropolitan Growth & Dev. Cor.	12/8	26,000.00	12/1/97	10.528%	
Texas Certified Dev. Co. Inc.	12/8	43,000.00	12/1/97	10.528%	
Corp. for Econ. in Des Moines	12/8	44,000.00	12/1/97	10.528%	
Iowa Business Growth Co.	12/8	47,000.00	12/1/97	10.528%	
St. Louis Local Dev. Co.	12/8	51,000.00	12/1/97	10.528%	
N. Regional Planning Comm.Inc.	12/8	63,000.00	12/1/97	10.528%	
Wisconsin Bus. Dev. Fin. Corp.	12/8	99,000.00	12/1/97	10.528%	
Citywide SBD Corp.	12/8	115,000.00	12/1/97	10.528%	
Commonwealth SBD Corp.	12/8	162,000.00	12/1/97	10.528%	
Northshore Bus. Fin. Corp.	12/8	168,000.00	12/1/97	10.528%	
Cleveland Area Dev. Fin. Corp.	12/8	289,000.00	12/1/97	10.528%	
Greater Muskegon Ind. Fund Inc.	12/8	462,000.00	12/1/97	10.528%	
Bedco Development Corp.	12/8	500,000.00	12/1/97	10.528%	
Grand Rapids Local Dev. Corp.	12/8	81,000.00	12/1/02	10.559%	
Texas Certified Dev. Co. Inc.	12/8	104,000.00	12/1/02	10.559%	
Ocean State Bus. Dev. Auth Inc.	12/8	162,000.00	12/1/02	10.559%	
San Antonio Local Dev. Co. Inc.	12/8	165,000.00	12/1/02	10.559%	
Iowa Business Growth Co.	12/8	270,000.00	12/1/02	10.559%	

*maturity extension

DECEMBER 1982 ACTIVITY

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual	INTEREST RATE (other than semi-annual)
State & Local Development Company Debentures (Cont'd)					
Arvin Development Corp.	12/8	$ 322,000.00	12/1/02	10.559%	
Bay Area Employment Dev. Co.	12/8	328,000.00	12/1/02	10.559%	
South Shore Economic Dev. Corp.	12/8	349,000.00	12/1/02	10.559%	
Texas Certified Dev. Co. Inc.	12/8	386,000.00	12/1/02	10.559%	
City-Wide SBD Corp.	12/8	416,000.00	12/1/02	10.559%	
Columbus Countywide Dev. Corp.	12/8	30,000.00	12/1/07	10.569%	
Wisconsin Bus. Dev. Fin. Corp.	12/8	42,000.00	12/1/07	10.569%	
Saint Paul 503 Local Dev. Co.	12/8	42,000.00	12/1/07	10.569%	
Lawndale Local Dev. Corp.	12/8	75,000.00	12/1/07	10.569%	
Econ. Dev. of Sacramento	12/8	89,000.00	12/1/07	10.569%	
Birmingham City Wide LDC	12/8	92,000.00	12/1/07	10.569%	
Springfield Cert. Dev. Co.	12/8	126,000.00	12/1/07	10.569%	
Saint Paul 503 Local Dev. Co.	12/8	131,000.00	12/1/07	10.569%	
Evergreen Comm. Dev. Assoc.	12/8	168,000.00	12/1/07	10.569%	
Bay Area Employ. Dev. Co.	12/8	187,000.00	12/1/07	10.569%	
Brattleboro Dev. Credit Corp.	12/8	200,000.00	12/1/07	10.569%	
La Habra Local Dev. Co. Inc.	12/8	242,000.00	12/1/07	10.569%	
Wisconsin Bus. Dev. Fin. Corp.	12/8	260,000.00	12/1/07	10.569%	
San Diego County LDC	12/8	500,000.00	12/1/07	10.569%	
Bay Coloney Dev. Corp.	12/8	500,000.00	12/1/07	10.569%	
Columbus Countywide Dev. Corp.	12/8	500,000.00	12/1/07	10.569%	
TENNESSEE VALLEY AUTHORITY					
Seven States Energy Corporation					
Note A-83-03	12/30	447,425,024.26	3/31/83	8.509%	
DEPARTMENT OF TRANSPORTATION					
Section 511					
Milwaukee Road #2	12/22	999,984.00	6/30/06	10.747%	

FEDERAL FINANCING BANK
December 1982 Commitments

BORROWER	AMOUNT	GUARANTOR	COMMITMENT EXPIRES	MATURITY
El Salvador	16,500,000.00	DOD	11/30/84	11/30/94
Honduras	9,000,000.00	DOD	11/30/84	11/30/94
Morocco	20,000,000.00	DOD	11/30/84	11/30/94
Turkey	150,000,000.00	DOD	11/30/84	11/30/12
Pomonna, CA	1,500,000.00	HUD	8/1/84	8/1/84

FEDERAL FINANCING BANK HOLDINGS
(in millions)

Program	November 30, 1982	December 31, 1982	Net Change 12/1/82-12/31/82	Net Change 10/1/82-12/31/82
On-Budget Agency Debt				
Tennessee Valley Authority	$ 12,545.0	$ 12,640.0	$ 95.0	$ 355.0
Export-Import Bank	13,953.9	14,176.7	222.7	222.7
NCUA-Central Liquidity Facility	135.3	103.0	-32.3	-27.1
Off-Budget Agency Debt				
U.S. Postal Service	1,221.0	1,221.0	-0-	-0-
U.S. Railway Association	191.5	194.3	2.7	-.6
Agency Assets				
Farmers Home Administration	53,661.0	53,261.0	-400.0	-475.0
DHHS-Health Maintenance Org.	114.3	116.8	2.5	-14.3
DHHS-Medical Facilities	148.8	148.8	-0-	3.0
Overseas Private Investment Corp	21.5	19.4	-2.2	-2.2
Rural Electrification Admin.-CBO	3,123.7	3,123.7	-0-	-0-
Small Business Administration	56.7	56.1	-.6	-2.0
Government-Guaranteed Loans				
DOD-Foreign Military Sales	11,990.5	12,279.1	288.6	843.2
DEd.-Student Loan Marketing Assn.	5,000.0	5,000.0	-0-	-0-
DOE-Geothermal Loans	40.9	40.9	-0-	4.3
DOE-Non-Nuclear Act (Great Plains)	426.0	476.5	50.5	136.5
DHUD-Community Dev. Block Grant	115.6	125.8	10.2	8.8
DHUD-New Communities	33.5	33.5	-0-	-0-
DHUD-Public Housing Notes	1,652.8	1,675.7	22.9	51.4
General Services Administration	420.1	419.1	-1.0	-1.4
DOI-Guam Power Authority	36.0	36.0	-0-	-0-
DOI-Virgin Islands	29.5	29.5	-0-	-0-
NASA-Space Communications Co.	782.4	814.3	31.9	56.5
Rural Electrification Admin.	16,750.2	17,156.7	406.5	875.2
SBA-Small Business Investment Cos.	731.6	732.1	.5	20.1
SBA-State/Local Development Cos.	59.6	67.4	7.8	19.0
TVA-Seven States Energy Corp.	1,246.1	1,257.2	11.1	-.7
DOT-Amtrak	855.4	855.0	-.4	-.4
DOT-Section 511	187.1	188.0	1.0	-4.9
DOT-WMATA	177.0	177.0	-0-	-0-
TOTALS*	$ 125,707.0	$ 126,424.4	$ 717.4	$ 2,067.2

*figures may not total due to rounding

TREASURY NEWS
epartment of the Treasury • Washington, D.C. • Telephone 566-2041

For Release Upon Delivery
Expected at 2 p.m. EST
February 28, 1983

STATEMENT OF
THE HONORABLE JOHN E. CHAPOTON
ASSISTANT SECRETARY
(TAX POLICY)
DEPARTMENT OF THE TREASURY
BEFORE THE
SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION
AND THE
SUBCOMMITTEE ON OVERSIGHT OF THE INTERNAL REVENUE SERVICE
OF THE
SENATE FINANCE COMMITTEE

Messrs. Chairmen and Members of the Subcommittees:

I am pleased to have the opportunity to present the views of the Treasury Department on S. 446, S. 495, and S. 527. All three of these bills deal with the tax treatment of farmers who participate in the Administration's Payment-in-Kind (PIK) program. Although we have some technical comments on the bills as currently drafted, the Treasury Department strongly supports legislation which would remove any disincentives in current tax law to farmers' participation in the PIK program.

BACKGROUND

The PIK program is a land diversion program designed to reduce the amount of certain agricultural commodities in the marketplace, thereby raising the prices of such commodities. Under the PIK program, the Department of Agriculture will compensate a participating farmer for removing acreage from active production by giving the farmer a percentage of the amount of the commodity he otherwise could have grown. The commodity is to be available to the farmer at the time of normal harvest, although the government will pay storage costs for up to five additional months.

Income Tax Consequences

Under current income tax law, a farmer would realize gross income from this transaction equal to the amount of the fair market value of the commodity received at the time the commodity is made available to him. The farmer would take a tax basis in the commodity equal to the amount included in income. He would recognize additional income (or loss) from the sale of the commodity if the amount realized from such sale exceeds (or is less than) the amount already included in income. Further, the farmer would be entitled to deduct his basis in the commodity to the extent it is used for feed.

The current law income tax treatment of the transaction involved in the PIK program is more complicated in the case of farmers who have nonrecourse loans outstanding from the Commodity Credit Corporation (CCC) secured by commodities which they either store on their own premises or in warehouses. The Department of Agriculture proposes to implement the PIK program for these farmers in two steps, as follows:

(1) the CCC will purchase the commodity from the farmer for an amount equal to the outstanding loan which is secured by the commodity, and the loan will thereby be discharged; and

(2) the CCC will then deliver that exact commodity or, in the case of farmers whose commodities are stored in warehouses, the warehouse receipt representing the commodity, to the farmer as his payment-in-kind under the PIK program.

The income tax consequences to a farmer in these circumstances would depend upon whether the farmer has made an election under section 77 of the Internal Revenue Code to treat the nonrecourse loan from the CCC as a sale for tax purposes. If the farmer makes a section 77 election, the loan proceeds are included in the farmer's income in the year of receipt. Since a farmer who has made a section 77 election has already been taxed on the proceeds of his CCC loan, the cancellation of that loan in exchange for the commodity securing the loan would have no further tax consequences to the farmer. The subsequent transfer of the commodity back to the farmer would be subject to the same tax treatment as described above; that is, the farmer would have gross income equal to the fair market value of the commodity when it is made available to him and would take a basis in the commodity equal to that value.

In the case of farmers who do not make a section 77 election, the CCC loan, when made, is treated as a loan rather than a sale. Therefore, the PIK transaction would be treated as a sale of the commodity for an amount equal to the outstanding debt which the commodity secured, followed by receipt of the commodity as a PIK payment. The result would be that the farmer would be taxed first on the amount of the debt which was discharged in the sale transaction and second on the amount of the fair market value of the commodity received in the PIK transaction. However, as discussed above, the farmer would take a basis in the commodity received equal to its value.

Estate Tax Consequences

Under section 2032A of the Internal Revenue Code, if certain requirements are met, real property which is used as a family farm and which passes to or is acquired by a qualified heir may be included in a decedent's estate at its current use value, rather than its full fair market value. Among the requirements which must be satisfied are: (1) the property must have been owned by the decedent or a member of his family and used "as a farm for farming purposes" on the date of the decedent's death and for periods aggregating five years or more during the eight-year period ending with the decedent's death; and (2) there must have been "material participation" in the operation of the farm by the decedent or a member of his family for periods aggregating five years or more out of the eight-year period ending on the date of the decedent's death.

Section 2032A also provides that the estate tax benefit of special use valuation generally is recaptured if the qualified heir disposes of the property to a nonfamily member or ceases to use the property "as a farm for farming purposes" within 10 years after the decedent's death and before the qualified heir's death. With certain exceptions, the qualified heir ceases to use the property for the qualified farming use if he or members of his family fail to participate materially in the farm operation for periods aggregating more than three years during any eight-year period ending after the decedent's death and before the qualified heir's death.

Another estate tax provision relevant to many farmers participating in the PIK program is section 6166 of the Code, which allows deferred payment of estate tax attributable to qualifying closely held business interests owned by decedents. The benefits of section 6166 are limited to interests in active trades or businesses.

A question may arise whether property on which a cash crop is not being grown as a result of participation in the PIK program, or in some other acreage-reduction program sponsored by the Department of Agriculture, is nevertheless being used "as a farm for farming purposes" within the meaning of section 2032A. Similar questions may be posed as to whether there has been the requisite "material participation" for purposes of section 2032A and whether the property is part of an active trade or business qualifying for estate tax deferral under section 6166.

Although none of these estate tax questions is specifically addressed in the present statute or regulations, we believe that the dedication of land to an acreage-reduction program sponsored by the Department of Agriculture generally will not prevent satisfaction of the requirements of section 2032A or section 6166 under present law. As I indicated in my testimony delivered before the Select Revenue Measures Subcommittee of the House Ways and Means Committee last Wednesday, February 23, we initially had some question about the result in cases where a farmer removes his entire farm from active production under an acreage-reduction program sponsored by the Department of Agriculture. Based on our further study of the issues involved, however, we are now of the view that land dedicated to such a program should be considered as used for farming purposes and that material participation in such a program should be viewed as material participation in an active farming business for all relevant tax purposes. I anticipate that the Internal Revenue Service will issue a formal announcement this week to confirm this treatment under current law.

DESCRIPTION OF S. 495

S. 495 is identical in all relevant respects to H.R. 1296, a bill on which I testified on Wednesday, February 23, before the Subcommittee on Select Revenue Measures of the House Ways and Means Committee. At that hearing I expressed Treasury's strong support for legislation adopting the general policy position of H.R. 1296 and S. 495, although I noted a number of technical comments on the bill. A copy of my written statement before the Select Revenue Measures Subcommittee is attached to this statement. In light of my previous testimony, I will confine the balance of my remarks today to the other two bills, S. 446 and S. 527.

DESCRIPTION OF S. 446 AND S. 527

Income Tax Provisions

S. 446 would amend section 451 of the Code, which relates to the taxable year income is to be taken into account for tax purposes, by providing that no income would be realized upon the receipt or right to receive any commodity under a certified payment-in-kind program (which would include the current PIK program), but that income would be realized from a subsequent sale or exchange of such commodity. For purposes of determining the amount realized from such sale or exchange, the farmer would have a zero tax basis in the commodity and the character of the income from the sale or exchange would be ordinary. S. 527 contains similar provisions. In addition, S. 527 provides that the cost basis of a taxpayer's payment in kind will be zero for all purposes of the Code, and that the character of the gain realized from the sale or exchange of the payment in kind (or any property the basis of which is determined by reference to the basis of the payment in kind) will be taxed in the same manner as a crop grown by the taxpayer.

S. 527 also provides that where farmers have outstanding CCC loans, the tax treatment of the receipt of the payment in kind will be determined without regard to any related transaction involving the loan. Where a taxpayer has made an election under section 77 with respect to a loan, the loan aspect of the PIK transaction will be treated as the closing of the sale deemed made pursuant to the section 77 election. Where no section 77 election has been made, the taxpayer would be deemed to have sold the commodity securing the loan in exchange for a cancellation of the loan.

In addition, S. 527 addresses a number of ancillary income tax issues raised by the PIK program. The bill provides that for purposes of the Internal Revenue Code and the Social Security Act, any income received from the sale or exchange of a taxpayer's payment in kind will be treated as income from the trade or business of farming and that a taxpayer will be treated as engaged in the trade or business of farming with respect to any land diverted pursuant to the PIK program. With respect to a cash basis taxpayer, S. 527 provides that any amount a taxpayer is entitled to receive as reimbursement for storage will not be included in income until actually received by the taxpayer.

S. 527 also contains special rules for cooperatives which provide that any cooperative which markets a commodity received by, or on behalf of, a member or patron under a certified payment-in-kind program will be treated as marketing the product of such member or patron.

Estate Tax Provisions

S. 446 also would amend section 2032A of the Code to provide that any commodity received by a person under a certified payment-in-kind program shall be treated as having been produced by such person on the property dedicated to such program. The bill does not refer specifically to either the qualified use test or the material participation test.

S. 527 would add two new paragraphs to section 2032A to provide that property diverted from farm use for up to three years under a certified payment-in-kind program shall be treated as used for a qualified use. This bill has no corresponding provision, however, relating to the material participation test.

S. 446 has no provision which addresses the effect of the PIK program on section 6166. S. 527, on the other hand, provides that property used in the trade or business of farming shall not be treated as withdrawn from such trade or business if such property is diverted from use for farming purposes solely by reason of participation in a certified payment-in-kind program. This provision would not apply, however, in determining whether the estate of a farmer who died with all or a portion of his property withdrawn from active farm production pursuant to a certified payment-in-kind program would remain eligible for estate tax deferral under section 6166.

DISCUSSION

Timing of Income Recognition

Many farmers participating in the PIK program will have sold crops in the current taxable year which were harvested in a prior taxable year. Current law may impose a hardship on these taxpayers because they will have, in effect, income from two crops (the income from the prior year's crop that is sold, plus the income from the PIK payment) in the same taxable year. In addition, under current law, farmers participating in the PIK program will be under pressure to sell commodities to obtain cash to pay their income tax liabilities arising from the actual or constructive receipt of the PIK payments; and those sales may have to be made in a market flooded with commodities being sold by other farmers facing the same tax liquidity problem. These tax-motivated sales may cause farm commodity market problems of the type that the PIK program is designed to reduce. The potential tax and market problems also may discourage farmers from participating in the PIK program, thus frustrating Federal agricultural policy.

In view of these problems, the Treasury Department strongly supports changes in the current law which adopt the general policy position underlying S. 446 and S. 527. Because PIK payments, in effect, are replacements for the commodities which farmers could have been expected to produce from the normal use of land devoted to the program, the tax law should treat farmers who receive commodities under the program as if they had grown the commodities themselves. Under this approach, farmers would recognize income only in the year they actually sell or otherwise dispose of the commodities in question. However, as I indicated earlier, we do have some technical comments on the bills as currently drafted.

First, we do not believe that the legislation should be drafted as an amendment to section 451 of the Code. Section 451 relates to the timing of the recognition of income depending upon the taxpayer's method of accounting. Under either the cash or accrual method of accounting, a PIK payment would be recognized for tax purposes in the year the farmer receives or has a right to receive the payment. The issue is not one of timing but one of income inclusion. We believe that the bill should be drafted to provide an exclusion from gross income for commodities received under the PIK program and, further, to provide that those commodities will have a zero basis for income tax purposes.

Second, we believe any bill enacted by Congress in this area should make it clear that a taxpayer will have a zero cost basis in any commodity received under the PIK program for all purposes of the Code and not just on the sale or exchange of the commodity. While S. 527 accomplishes this result, S. 446 does not.

Third, the questions whether PIK payments should be treated as if farmers had grown the commodities themselves and whether farmers who divert some or all of their acreage under the PIK program should be considered as engaged in the trade or business of farming are questions that have ramifications for a number of other provisions of the Code. For instance, section 447 provides special accounting rules for corporations engaged in the trade or business of farming.

Section 175 provides special treatment for soil and water conservation expenditures for taxpayers engaged in farming. Tax exempt farmers' cooperatives could lose their exemptions if the commodities received by their members and assigned to the cooperatives were not treated as produced by the members. Moreover, a determination of the self-employment income of a farmer who diverts acreage pursuant to the PIK program also depends on whether the farmer is deemed to participate materially in the production of farming commodities or the management of that production.

We believe that farmers who receive PIK payments should be treated as if they had grown the commodities received for all purposes of the Code and that participation in a Department of Agriculture program should be treated as a farming activity. We believe this result can be reached in most cases under current law. However, the legislation should address these ancillary issues to the extent that current law needs to be clarified to ensure appropriate results. S. 527 addresses these ancillary issues, but S. 446 does not.

Estate Tax Consequences

Treasury generally supports legislation which would make it clear to farmers that participation in the PIK program will not adversely affect their eligibility for special use valuation under section 2032A or estate tax deferral under section 6166. We believe that any such legislation should apply to the pre-death qualification requirements of these two sections as well as the post-death recapture provisions of section 2032A(c) and acceleration provisions of section 6166(g).

Neither S. 446 nor S. 527 addresses all these concerns. With respect to section 2032A, S. 446 simply provides that a person who receives a crop pursuant to a certified payment-in-kind program will be treated as if he had grown the crop. While the language of the bill reflects the general approach which we believe is correct, some additional and more specific language relating to the qualified use and material participation tests may be desirable. S. 527 has the desired specificity for the qualified use test, but does not deal with the material participation test.

As noted above, S. 446 has no provision dealing with section 6166 whatsoever. S. 527 adequately addresses the post-death concerns by providing, in effect, that participation in the PIK program cannot cause an acceleration of estate tax deferred under section 6166. S. 527 fails, however, to cover the equally important pre-death qualification test of this section. If legislation is desired to clarify the results under section 6166, the bill should contain a comprehensive provision addressing all relevant concerns.

CONCLUSION

In conclusion, I would like to reiterate Treasury's strong support of legislation that will remove any impediment to the successful operation of the PIK program which current tax law may create. While I have noted some technical comments on the bills as currently drafted, I am confident that we can work out a satisfactory solution to these problems with the Subcommittees.

I would be happy to answer your questions.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. March 1, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $ 12,400 million, to be issued March 10, 1983. This offering will provide $950 million of new cash for the Treasury, as the maturing bills are outstanding in the amount of $ 11,453 million, including $952 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and $2,494 million currently held by Federal Reserve Banks for their own account. The two series offered are as follows:

91-day bills (to maturity date) for approximately $6,200 million, representing an additional amount of bills dated December 9, 1982, and to mature June 9, 1983 (CUSIP No. 912794 CX 0), currently outstanding in the amount of $ 5,822 million, the additional and original bills to be freely interchangeable.

182-day bills (to maturity date) for approximately $ 6,200 million, representing an additional amount of bills dated September 9, 1982, and to mature September 8, 1983 (CUSIP No. 912794 DC 5), currently outstanding in the amount of $ 7,127 million, the additional and original bills to be freely interchangeable.

Both series of bills will be issued for cash and in exchange for Treasury bills maturing March 10, 1983. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, March 7, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on March 10, 1983, in cash or other immediately-available funds or in Treasury bills maturing March 10, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
Wednesday, March 2, 1983

Contact: Charley Powers
(202) 566-2041

TREASURY ISSUES WITHHOLDING RULE REVISIONS

The Department of the Treasury today announced revisions to the regulations regarding withholding on dividends and interest and on the broadened information reporting rules, to take into account concerns raised by Members of Congress and affected financial institutions.

The announcement states that Treasury will defer the effective date for withholding with respect to original issue discount instruments until January 1, 1984. The Treasury stated that it recognized that withholding on original issue discount before that time would result in undue hardship to institutions. Similar relief is provided concerning the new information reporting requirements. All other withholding provisions are effective July 1, 1983. Treasury and the Internal Revenue Service will commence publication of information regarding outstanding original discount instruments in June 1983.

Today's other revisions relate to: payee unknown, year-end withholding, transactional reporting, nominees, and backup withholding.

"The Administration remains committed to the withholding provisions," said Treasury Secretary Donald T. Regan. "We think it is the most effective means of improving the collection of taxes on unreported interest and dividend income. We believe that the changes described in today's announcement and forthcoming regulations will go far to respond to the concerns raised by the financial industry. They will simplify the operation of the withholding rules. We look forward to continuing to work with the industry to assure that withholding goes into effect on July 1 with minimum disruption."

The announcement is attached.

R-2037

See corresponding letter, following Press Release #2063, from Regan to Dole

The Treasury Department and the Internal Revenue Service are completing their review of the comments received regarding the regulations under the interest and dividend withholding and broadened information reporting provisions of the Tax Equity and Fiscal Responsibility Act of 1982. It is expected that these regulations, revised to take into account the comments received, will be published as final regulations in the near future. Proposed regulations concerning the allocation of the credit for tax withheld from interest and dividends among trusts and estates and their beneficiaries will be published shortly thereafter.

Discussed below are some of the areas in which the withholding and information reporting regulations will be revised.

(1) Original Issue Discount. A number of persons expressed concern that payors would be unable to determine the amount subject to withholding with respect to instruments issued at a discount. The Treasury Department and Internal Revenue Service will take the following steps to insure that payors are able to calculate readily the original issue discount attributable to these instruments:

(a) Treasury Bills. Commencing June 15, 1983, the Treasury will publish on a quarterly basis a list showing the original issue discount (based on the noncompetitive price), maturity date, and CUSIP number for Treasury bills maturing during the following quarter. Attached is a sample schedule setting forth the information which will be provided. This information will enable payors to determine readily the amount of discount income associated with Treasury bills. Persons are encouraged to comment on the format for presenting this information.

(b) Other Discount Instruments. On June 15, 1983, the Internal Revenue Service will commence publication of information concerning outstanding publicly-traded discount instruments. The publication will provide the following information: (i) for long-term discount instruments (maturities in excess of 1 year), the name of the issuer, identification of issue, date of issue, and amount of discount to be reported to a holder during the calendar year; and (ii) for short-term instruments (not exceeding 1 year), the name of the issuer, identification of issue, date of issue, issue price, redemption price and original issue discount. The withholding and information reporting regulations will relieve payors of liability for failure to withhold tax or furnish information on original issue discount on any instruments with respect to which information is not provided in the publication.

(2) Undue Hardship. Under the temporary and proposed regulations, applications for deferral of application of some or all of the withholding provisions were to be made, in general, not prior to April 1. A revenue procedure will be issued within a few days providing detailed information as to the circumstances under which an institution will be considered unable to comply with the withholding provisions without undue hardship, thereby qualifying for deferral of some or all of the withholding provisions (but, in accordance with the law, not beyond December 31, 1983). A rule will be provided concerning the availability of relief under this provision with respect to the requirement of withholding on original issue discount. Many persons have commented that it will be difficult or impossible to commence withholding on July 1 with respect to original issue discount. Although the publications described in (1) above ultimately will alleviate the problems of withholding on original issue discount, it is clear that payors generally will not be able to develop procedures for withholding on original issue discount by July 1, 1983 notwithstanding their efforts to do so. Accordingly, the Treasury Department will permit payors to delay the application of the withholding provisions to original issue discount until December 31, 1983 because of the undue hardship that would result from payors attempting to comply with such withholding requirements prior to that time. Payors will not be required to make application to the Internal Revenue Service to qualify for the delay in application of the withholding rules to original issue discount. Payors who are able to commence withholding on original issue discount prior to December 31 may do so, also without application to the Internal Revenue Service. The Internal Revenue Service also will consider the lack of information regarding original issue discount instruments to constitute reasonable cause for failure to comply with the expanded information reporting requirements added by the Tax Equity and Fiscal Responsibility Act of 1982 until December 31, 1983. The Internal Revenue Service previously stated that reasonable cause for failure to comply with these reporting requirements would be considered to exist for discount instruments until April 1 and July 1 in Announcement 83-6.

(3) Payee Unknown. Many financial institutions stated that it would be difficult to administer a rule requiring withholding upon payments with respect to which the institution is unable to determine the identity of the payee at the time the payment is first received. In many of these cases, institutions are able to identify the payee as an exempt recipient within a short time after receiving the payment. The final regulations will allow up to 60 days to confirm the ownership of payments in these situations before withholding will be required.

(4) Year-End Withholding. The final regulations will confirm that the election to defer withholding until year-end

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(4) Year-End Withholding. The final regulations will confirm that the election to defer withholding until year-end

will be available for regular savings accounts, interest-bearing checking accounts and their equivalents, including the new money market accounts and SUPER-NOW checking accounts.

(5) Transactional Reporting.

(a) Where an interest coupon or savings bond is presented to a middleman for payment, the regulations will provide that only the name of the middleman, and not the name of the issuer of the obligation, should be reported on Form 1099. In addition, one Form 1099 may be used to show all payments made as part of a single transaction irrespective of whether the payments are made on obligations of different issuers.

(b) Persons presenting coupons from tax-exempt obligations must certify in writing that interest represented by the coupon is tax-exempt. Payors can rely on such certifications in not withholding or filing information reports with respect to such coupons. A statement that interest coupons are tax-exempt on the envelope commonly used by financial institutions to process such coupons, signed by the taxpayer, will be sufficient for this purpose if the envelope is properly completed (i.e., shows the name, address and taxpayer identification number of the taxpayer).

(6) Nominees. The final regulations will provide that nominees may be treated as exempt recipients without being required to file an exemption certificate if the nominee is known generally in the investment community as a nominee or is listed in the American Society of Corporate Secretaries, Inc. Nominee List.

(7) Backup Withholding. The backup withholding provisions added by the Tax Equity and Fiscal Responsibility Act of 1982 will not apply to payments of interest, dividends or patronage dividends that are within the scope of the 10 percent withholding provisions. The backup withholding provisions will not apply even if one or more exceptions to the 10 percent withholding rules applies to the payment (such as the exception for payments to exempt recipients, exempt individuals, and the minimal interest payment exception).

MATURITY DATE		CUSIP	EARLIEST ISSUE DATE	NONCOMPETITIVE PRICE	ORIGINAL ISSUE DISCOUNT
		912794			
March	3	CL6	9/2/82	95.073	4.927
	10	CM4	9/9/82	95.144	4.856
	17	CN2	9/16/82	95.094	4.906
	24	CA0	3/25/82	87.352	12.648
	31	CP7	9/30/82	95.351	4.649
April	7	CQ5	10/7/82	95.334	4.666
	14	CR3	10/14/82	96.090	3.910
	21	CB8	4/22/82	87.128	12.872
	28	CS1	10/28/82	95.717	4.283
May	5	CT9	11/4/82	95.839	4.161
	12	CU6	11/12/82	95.778	4.222
	19	CC6	5/20/82	87.671	12.329
	26	CV4	11/26/82	95.923	4.077
June	2	CW2	12/2/82	95.697	4.303
	9	CX0	12/9/82	95.827	4.173
	16	CD4	6/17/82	87.692	12.308
	23	CY8	12/23/82	95.903	4.097
	30	CZ5	12/30/82	95.930	4.070
July	7	DH4	1/6/83	95.983	4.017
	14	DA9	7/15/82	87.545	12.455
	21	DJ0	1/20/83	96.093	3.907
	28	DK7	1/27/83	95.883	4.117
Aug.	4	DL5	2/3/83	95.842	4.158
	11	DB7	8/12/82	88.681	11.319
	18	DM3	2/17/83	95.759	4.241
	25	DN1	2/24/83	95.969	4.031

File

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

STATEMENT BY DONALD T. REGAN
SECRETARY OF THE TREASURY
WEDNESDAY, MARCH 2, 1983

We have announced today revisions to the regulations regarding withholding on interest and dividends in response to the concerns raised by financial institutions and many Members of Congress.

I met this morning with Congressional leaders -- Howard Baker, Bob Dole, Dan Rostenkowski, Bob Michel, Barber Conable and a representative of Speaker O'Neill -- and discussed these revisions with them.

All of them reaffirmed their commitment to withholding and expressed their determination to oppose any attempt to repeal it. It seems clear that the leadership, as well as other Members of Congress, are convinced that withholding is a reasonable approach that must be maintained.

"We believe today's announcement and the forthcoming regulations respond to the legitimate concerns raised by the financial industry and individuals," Senator Howard Baker said in the meeting this morning.

We will continue to work with the industry, but we will not back off of withholding. It is the most effective means of collecting taxes which are owed but not being paid.

R-2055 - See corresponding letter, following Press Release # [illegible], from Regan [illegible]

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

REMARKS BY
R.T. MCNAMAR
DEPUTY SECRTARY OF THE TREASURY
BEFORE THE
NATIONAL ASSOCIATION OF MUTUAL SAVINGS BANKS
MONDAY, FEBRUARY 28, 1983
WASHINGTON, D.C.

Framework for the Future

Good afternoon. It's a pleasure for me to meet with you today. Last November I wrote to Saul that I hoped The Mutual Savings Banks would consider some of our views on deregulation. He said, "We'll do even better. Come speak at our February meeting and make your case." So here I am.

I was going to bring along some exemption forms for withholding of dividends and interest. But somehow that didn't seem like the right foot to get off on to discuss deregulation so I'll move right into deregulation with a somewhat more congenial set of opening remarks about the economy.

First, inflation is down, interest rates are down, oil prices are falling, and the general health of your industry seems much improved. That's good news for all of us.

After more than a year of wrong economic projections, conflicting economic indicators, and many disappointments during the recession, today I feel fairly confident in saying that the recovery has in fact started. However, I am reminded of the joke President Reagan tells about the guy at the Halloween party who put egg on his face and went as an economist.

Somehow that line is a little funnier now than it was a few months ago when the recession seemed darkest. But now we do see numerous signs of improvement -- from a 21 percent prime to a 10.5 percent prime, from 12 percent inflation to something between 2 and 4 percent.

R-2059

Of course, we're never totally out of the woods with inflation. It lurks in the trees like a cagey old coyote, and I urge all of you to remember its ravages on your industry as we hear the occasional cries for loose money or "just a little more inflation." It's still the villian that has produced today's record high real interest rates, and can scare interest rates back up -- and that we don't need.

Nevertheless, today we are in a much better economic climate. We have made considerable progress in meeting the original economic objectives of this Administration.

As this audience knows, one of the basic laws governing the financial industry, the Glass Steagall Act, was rolled out of Congress about the same time Henry Ford revolutionized the auto industry with the Model A. Both were great accomplishments. But today we wouldn't expect a Model A to compete at Indy. Likewise we should't expect the financial industry's laws of the 1920's to be appropriate for the end of the 20th Century.

The auto industry has come a long way since the Model A. Well, the thrift industry has also come a long way, but we're only part way to where we will be.

As you know, last year the Administration sent a proposal to the 97th Congress that would have allowed bank holding companies through subsidiaries to offer a broad range of services. This legislation sought to enhance further the competitive ability of traditional depository institutions. Although it was not voted on in the 97th Congress, we will be reintroducing the legislation this year.

We all recognize the importance of keeping safety and soundness in the financial services industry. So the goal of that legislation is to define a framework for financial institutions where they can take banking risks and other financial or commercial risks. Thus, a broader range of services can be offered while insuring the soundness of the system, fostering competition, and permitting individual companies to make decisions about their own business strategies. In short, to permit managers and institutions to succeed of fail on their own.

Getting this kind of legislation passed into law will not be easy. We'll need your help and the support of the entire financial industry. We think it's in all of our interest to put the legislative framework in place during a time of recovery.

Our proposal would allow bank holding companies, through subsidiaries, to engage in any additional activities "of a financial nature." For example, the bill would authorize bank holding company subidiaries to engage in insurance underwriting and brokerage; real estate investment, development, and brokerage. In the securities field, bank holding company subsidiaries could deal in and underwrite U.S. and most state and municipal securities, including revenue bonds. They could sponsor, control and advise an investment company and they could deal in and distribute bank certificates of deposit and commercial paper of its parent holding company or any of the holding company's subsidiaries.

By allowing bank holding companies, rather than banks themselves, to offer a broader range of services, the Administration's holding company proposal accomplishes certain legitimate policy objectives of bank regulation while allowing banks to associate themselves with firms that can compete for customers with other diversified financial services.

In the Administration's view, permitting direct entry by banks themselves into non-banking activities would be unsound policy for two principal reasons. First, allowing banks to offer non-banking services would create opportunities for unequal competition. Second, by subjecting banks to new commercial risks, it might jeopardize their safety and soundness. Thus, the rationale for the upstream holding company.

Upstream holding companies are, of course, legally separate from banks they own and control, and the capital invested in a holding company's non-banking subsidiaries is not the subsidiary banks' capital. Rather, it is the capital raised by a holding company in competition with other borrowers in the credit markets, i.e., at a competitive, market-determined rate.

This, in itself, helps insulate banks against threats to their safety and soundness. Permitting holding companies to offer a broader range of services can also contribute in a positive way to the financial soundness of its subsidiary banks. Holding companies were originally viewed as sources of strength for their subsidiary banks, and this would certainly be the case if they were engaged in profitable non-banking activities. (Obviously, poor management would make the opposite true.)

During times of strain on subsidiary bank's resources, a soundly financed and profitable holding company could furnish additional equity capital to the bank. And, holding companies may acquire substantial tangible assets, e.g., real estate that can provide holding company management with tax and management opportunities to borrow monies at the holding company level using the assets as security for repayment of the borrowed funds. Holding company debt can be converted into an equity investment that is infused in the down-stream bank, S&L, insurance company, or other financial services activity. Thus, the opportunities to raise new capital to support traditional financial services can be enhanced. But, obviously by contrast, holding companies can hardly be expected to contribute significantly to bank soundness if their range of activities does not extend beyond what is permitted to banks themselves.

During the most recent session of Congress, the principle that holding companies should be allowed to expand into activities otherwise forbidden to banks was finally accepted. In passing the Export Trading Company Act, Congress authorized bank holding companies to own export trading companies -- firms that would purchase goods and services in the United States and sell them abroad. But the Act specifically excluded banks from such ownership. This commercial dealing activity, is from a public policy standapoint far too risky for banks themselves. Hence, it was authorized for bank holding companies because these entities are legally separate from their subsidiary banks and because their commercial activities would not create risks for their subsidiary banks.

The public policy objective of the holding company structure is to have functionally equivalent competitive activities capitalized by equivalent market sources and at equivalent costs for the venture. In modern stock portfolio practice, this would be a variant of the beta theory of stock volatility reflecting the variability of earnings. It is precisely for these reasons that the Administration is unalterably opposed to these additional powers being in downstream holding companies of so-called service corporations under a bank, savings and loan or mutual savings bank. For a mutual savings bank that would provide federally insured low cost capital for non-savings bank activities.

The underlying purpose of the Adminstration proposal, then, is to permit banks -- if they choose -- to become part of diversified financial services firms so that they will be able to adapt to and compete in a rapidly evolving market. By utlizing the bank holding company framework, the proposal seeks to expand the range of services that banking organizations are associated with, without exposing banks themselves or their capital to the risks of non-banking activities.

The Administration's proposal enhances competitive equality because any organization performing only activities in which a bank holding company may engage, may itself organize a holding company and acquire a subsidiary bank or banks, or other service firm. As a result, deregulation of bank holding companies is a two-way street with banks able to expand into other financial businesses and competing firms able to expand into banking.

At this point, you may ask why should mutual savings banks care about or support a bill for commercial banks and commercial bank holding companies? The answer is two-fold. First, some mutual savings banks and savings and loans will wish to consider converting to a stock form to take advantage of the additional financial services powers that will someday be available through a holding company. Others, and perhaps most, will not. However, they also have a stake in ensuring that the lines of competition between S&Ls, mutual savings banks, and commercial banks are fairly drawn. And this means that a mutual savings bank trustee should be concerned that the stock form of an S&L or a commercial bank not have an unfair advantage by engaging in other activities through the bank itself or a service corporation that pyramids the S&L or bank's capital in ways or businesses that are prohibited by the mutual savings bank. Thus, even a mutual savings bank that does not plan to change its form should have an interest in ensuring that the government's legal framework for commercial banks and S&Ls doesn't provide the stock form of ownership with unfair competitive advantages in the mutual savings banks' competitive arena.

Too many organizations view the proposed new activities for banks as an intrusion into their business rather than an invitation for them to expand into banking. And, I fear those who object are either ignoring change or giving credence to the old adage that "businesssmen love competition, but hate to compete."

Finally, let's dwell for a moment on how all these changes might specifically influence the mutual savings bank industry.

We hope that the high inflation, high interest rate environment of the last few years is behind the savings bank industry. The Garn-St Germain Act should help the industry remain viable while it rebuilds its surplus and deposits which were so seriously depleted during this period.

As the savings bank industry begins its recovery, it needs to think about its future. The industry will need time to rebuild its surplus and deposits or customer base.

At the same time, it will be crucial for mutual savings banks to decide what kinds of institutions you want to be and which customers you want to serve. Most of you will not be able to do all things for all people and rebuild your earnings power and net worth at the same time.

Mutual savings banks have long been recognized as more bank-like than S&Ls despite your large mortgage portfolios. This difference is recognized in the industry's expanded authority for commercial lending and in its tax treatment. In the future, does the mutual savings bank industry want to be more like commercial banks, or more like S&Ls or something in between? Your proposed merger with the Mutual Savings and Loan League suggests both are giving serious consideration to what you will look like in the future.

What other types of activities are MSBs interested in pursuing? Some have indicated an interest in the mutual fund business, and I am sure there are other activities that other institutions are examining. The Administration is also concerned about the future of the savings bank industry.

The Garn-St Germain Act of 1982 authorizes Federal Mutual Savings Banks to make commercial loans equal to 15 percent of assets and consumer loans equal to 30 percent of assets.

To expand these activities fully, MSBs will have to develop management and markets that can produce real profits. This will not be easy given the location of the industry in the same markets as the strongest commercial banks. It, therefore, seems very important that individual MSBs define their goals very clearly.

While the future presents many challenges for the industry, it also presents many opportunities. A recovery of the housing market has already begun and MSBs should be able to take advantage of the recovery to restore profitability to the major segment of their business. Real estate finance is an area the industry knows well and should be able to serve profitably very quickly.

The money market deposit account affords the industry an excellent opportunity to serve retail customers who now have a renewed interest in saving at thrift institutions. The funds and customers gained through the use of this popular account should be retained with more expansive credit programs. Herein lies an opportunity to fund expanded consumer lending.

Without the interest rate differential, thrift institutions will have to offer more services to retain their customers. The purpose of the Garn-St Germain Act was to give you the authority to more effectively expand your services. But the lack of the differential makes it an absolute necessity.

For those MSBs who can build on their real estate business with commercial lending or who have a good potential with small business customers, your increased consumer lending powers should be helpful. This is just one more arrow in your sling.

I know some members of your industry that have shown great interest in our bank holding company proposal for expanded commercial bank activities. This proposal did not include thrift institutions which have just obtained extensive new commercial lending powers.

Given the condition of the thrift industry, we think it ought to focus on rebuilding its existing business and developing those activities already authorized under the Garn-St Germain Act. After that, and as soon as possible, I personally believe thrift institutions should be able to take on some of the additional financial services activities that we are proposing for commercial banks so they can compete with non-depository financial organizations.

TREASURY NEWS
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REMARKS BY
THE HONORABLE JOHN E. CHAPOTON
ASSISTANT SECRETARY
(TAX POLICY)

ANNUAL MEETING OF
THE ASSOCIATION FOR ADVANCED LIFE UNDERWRITING
WASHINGTON, D.C.
March 1, 1983

I am happy to be back before the annual meeting of the Association for Advanced Life Underwriting for a third time in as many years. When I first spoke to you in 1981, the Administration had already presented the President's Program for Economic Recovery. At that time, my comments focused on the tax proposals that were a major element of the President's program: the across-the-board reduction in individual tax rates and the accelerated cost recovery system (ACRS).

My discussion of the issues that related directly to the professional interests of this group was limited to administrative issues, primarily the tax treatment of the so-called "wraparound annuities." In late 1981, the Internal Revenue Service issued a ruling discussing the tax treatment of mutual fund wraparound annuities. Subsequently, the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") revised the rules governing withdrawals from annuities and imposed a five percent penalty on withdrawals made within 10 years of the purchase of most deferred annuities. The net effect of these changes is to preserve the benefit of deferral of tax on earnings through an annuity for traditional deferred annuity contracts, while denying much of this benefit where an annuity is used as a short-term investment vehicle. We think this is a satisfactory solution and we have no plans to seek any further changes in the tax treatment of annuities.

Last year in speaking to this group, my comments reflected the Administration's realization that certain Internal Revenue Code provisions affecting life insurance companies required repair. In particular, we recognized that the use of modified coinsurance was enabling most segments of the life insurance industry to obtain unintended tax benefits. The Administration's legislative proposal in the

R-2060

insurance area was limited: repeal section 820, which established special tax rules for modified coinsurance arrangements. I discussed with you our recognition that it might be appropriate to reexamine, in consultation with representatives of the life insurance industry, other Internal Revenue Code provisions affecting the taxation of life insurance companies. However, I stated our view that a broader revision should await a thorough examination of the proper method of taxing life insurance companies and life insurance products.

As you know, 1982 saw the enactment of significant legislation affecting life insurance companies and life insurance products. Many provisions adopted in 1982 apply only for a "stopgap" period, that is for taxable years 1982 and 1983. These stopgap provisions include interim changes sought by the life insurance industry until a more fundamental revision could be made to Subchapter L of the Internal Revenue Code. Also included in the stopgap provisions were statutory guidelines governing the characterization of Universal life insurance as life insurance for tax purposes. As mentioned, a permanent change in the tax treatment of annuities also was made.

The enactment of provisions that would remain in effect for only a two-year period was intended to give Congress sufficient time to design and enact permanent tax changes applicable to the life insurance industry. This means, however, that unless legislation is enacted during 1983, most of the stopgap provisions will expire, and this could create imbalances in the tax treatment of different life insurance products sold by competing segments of the industry.

Only ten months remain until stopgap runs out. During this period, Congress must consider many difficult and controversial tax matters, including social security issues. The legislative clock is running. Yet fundamental changes remain to be considered with respect to the tax treatment both of life insurance products and the industry itself. I hope that the industry, the Treasury and the tax-writing committees can work together in a timely manner to fashion the structural changes needed.

I would like to take the opportunity of my invitation to speak before you this year to outline several factors we think should be considered in formulating a permanent legislative replacement for the temporary Internal Revenue Code provisions adopted in 1982.

General Considerations

First, tax legislation affecting insurance companies and their products should reflect the significant changes in the operations of all financial intermediaries that has occurred in recent years. The enactment of the Garn-St. Germain bill in 1982 has expanded the powers of banks and savings and loan associations. In addition, the life insurance industry has been developing a variety of new products that contain predominantly investment features found in certificates of deposits, mutual funds and money market funds, as well as traditional insurance features.

Of course, the Administration remains committed to encouraging savings by individuals. Steady growth in long-term savings is essential to the continuation of our economic recovery. We are pleased with Internal Revenue Code changes which encourage increased savings, such as the increased availability of Individual Retirement Accounts.

Indeed, in the context of more long-term, comprehensive tax reform, a concern about increasing savings, which I share, might lead to the replacement of the current system with a tax on consumed income. Under this system, which could be far simpler than current law, deductions would be allowed for all saving, with the proceeds of all borrowing subject to tax. With a properly designed rate structure, this system could retain the same degree of progressivity as we have now, but within each income class those who save would pay less tax than those who spend.

It must be recognized, however, that while the existing tax system contains many features that are consistent with a consumed income tax, such as the exclusion from tax for savings through qualified retirement plans and IRAs, it is primarily a tax on income. The income earned on investments in mutual funds, bank and thrift deposits, and most other securities, generally is subject to tax when earned, unless it is exempted for certain well-defined policy reasons. For example, the investment income earned on tax deductible contributions to pension plans and Individual Retirement Accounts is effectively untaxed in order to encourage savings for retirement. It should be noted that these tax-favored forms of retirement savings are subject to significant restrictions, particularly in terms of the amounts that can be invested.

Taxation of Life Insurance Products

Historically, the income earned on investments made through life insurance generally has not been subject to federal income tax. The laudable social policy supporting this exemption is encouragement for individuals to protect their families against economic hardships that could result from premature death of the family breadwinners.

While we are not proposing to reconsider this rule or the policy it reflects with respect to traditional "garden variety" life insurance contracts designed primarily to protect against untimely death, it is plain that this historic treatment cannot be applied automatically to all arrangements offered by insurance companies, in light of the increasing investment orientation of the products offered by the life insurance industry. As an article pointed out in the Wall Street Journal only last week, life insurers are increasingly offering policies that look very much like investments offered by other financial institutions. In some policies, the traditional function of life insurance -- protection for the beneficiaries of the policy against the premature death of the insured -- is becoming a secondary factor. Yet the existing tax rules applicable to investments made through life insurance companies are markedly different from those applicable to investments made through other financial intermediaries. In most cases they are more favorable, and in many instances investments through life insurance companies are tax exempt. This distorts investment decisions and encourages the development of new life insurance products to take increasing advantage of an uneven playing field.

Consequently, in fashioning permanent tax legislation, we should recognize the similarity of these investment-oriented life insurance policies to other investments. One possibility might be to establish more favorable tax treatment for long-term savings generally (in addition to retirement savings) that could be offered by all financial institutions. It might be appropriate, or necessary for budgetary reasons, to delay taking such a step or to limit the amount that could be invested in tax-favored long-term savings plans, just as limitations are imposed on contributions to pension plans.

It also might be appropriate to restrict the types of life insurance policies that receive favorable tax treatment. In effect, a policy that is primarily an investment vehicle, particularly a short-term investment vehicle, would not be treated, for tax purposes, as life insurance. This approach is illustrated by TEFRA's provision governing the tax treatment of Universal life insurance: unless there is a sufficient element of insurance protection, the policy will not be subject to the favorable tax rules applicable to life insurance. Still another approach might be to bifurcate life policies that are weighted toward investment into the traditional whole life insurance feature and the investment feature, and limit the favorable life insurance tax rules to the insurance side of the arrangement. Of course, other approaches could be developed that would tend to equalize the tax treatment of comparable investments.

If it is determined that income from investment-oriented life insurance should be subject to taxation, it also would be necessary to determine whether the resulting tax should be collected directly from the policyholders, as generally occurs with respect to tax imposed on investment income, or collected from the life insurance company serving as a tax paying agent of the policyholders, with no tax being collected directly from the individual policyholders. This latter approach would reduce both the compliance and the paperwork burden on the companies. In form, this could be accomplished by imposing a supplemental tax on certain portions of the investment income of life insurance companies that would serve as a "proxy" for the tax that otherwise would be imposed at the policyholder level. The proxy tax rate could be set at a low rate that fairly approximates the average marginal tax rate of the policyholders.

A separate question that arises under the present tax rules for taxation of life insurance is whether tax benefits should be denied in the case of insurance arrangements (other than term insurance) designed to result in little net savings. For example, in TEFRA Congress treated certain borrowings from pension plans as taxable pension plan distributions. Similar policy questions arise from the expanding use of certain life insurance policies that emphasize the tax beneifts arising from systematic policy loans.

Taxation of Life Insurance Companies

Turning to the tax treatment of the life insurance companies, I believe that the tax rules to be put in place following expiration of the TEFRA stopgap provisions should not be based on an arbitrary division of a predetermined revenue target between the stock and mutual life insurance companies. In a fair tax system, competing products sold by mutual and stock life insurance companies should be subjected to comparable tax rates on comparable income.

Rather than focusing on revenue targets, the tax system applicable to the life insurance industry should focus on the correct measurement of economic income, even though mechanical approximations may be a practical necessity in certain instances. Under current law, the relationship between the industry's taxable income and its economic income is obscured. One cause of this obscurity is the present tax rules allowing reserves that significantly overstate the corresponding economic liability. It also results from tax provisions, including certain so-called "special deductions," that were designed to balance the industry's tax liability at a predetermined level and mix. If it is decided that the industry's tax liability is excessive, then adjustments should be explicit, rather than being made through the interplay of complex provisions of obscure origin that defy understanding and make analysis burdensome.

Conclusion

By building a short expiration date into the stopgap provisions of TEFRA, Congress guaranteed that policymakers would have to address issues of insurance taxation before the end of this year. I have attempted to set out some guiding principles which we will be using in our analysis, and I can assure you that we will temper them with pragmatism where necessary.

The life insurance industry has played a key role in the encouragement of personal savings through the provision of life insurance protection for many generations, and I am confident that the industry will continue to play this role for many generations to come. In changing the tax rules applicable to a changing industry, great care must be taken not to undermine this characteristic, particularly at a time when increased savings are so crucial to the future well-being of our nation.

TREASURY NEWS

epartment of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE UPON DELIVERY
EXPECTED AT 9:45 A.M.
Wednesday March 2, 1983

STATEMENT OF
THE HONORABLE JOHN E. CHAPOTON
ASSISTANT SECRETARY (TAX POLICY)
BEFORE THE
HOUSE BUDGET COMMITTEE TASK FORCE ON TAX POLICY

Mr. Chairman and members of the Committee:

It is a pleasure to meet with you today to discuss the Administration's contingency tax plan. The President included in his budget message a contingency tax plan in order to ensure financial markets, the business community, and the American taxpayer that future deficits -- which may occur after full economic recovery -- will not be excessive.

Like any other insurance program, the contingency tax plan is necessary for sound financial management. It provides certainty with respect to future deficit reductions if sufficient growth fails to keep those deficits within a tolerable range.

Also, as with any other insurance program, we earnestly hope that the conditions under which the contingency taxes would become effective never occur. If economic growth is sufficiently strong and government spending is sufficiently restrained over the next two or three years, then the contingency taxes will never be needed. However, it is because we cannot guarantee, with certainty, the rate of long-term growth in the economy that we need a contingency tax plan. In a very uncertain world this plan provides a measure of certainty that is necessary for orderly long-term financial and economic decisions that must be made by individuals and businesses alike.

R-2061

General Design of the Contingency Tax Plan

The contingency tax plan proposed by the President is designed to raise revenues -- and consequently reduce the deficit -- by about 1 percent of GNP, provided that Congress has adopted spending reduction proposals along the lines proposed by the Administration and that there is insufficient economic growth to keep the deficit below 2 1/2 percent of GNP. The contingency tax plan would go into effect on October 1, 1985, if the economy is growing on July 1, 1985, and if the forecasted deficit for fiscal year 1986 exceeds 2 1/2 percent of GNP. Chart 1 shows the effect on the deficit that the contingency taxes would have if they are implemented. It also shows how the budget picture would be altered by a much stronger expansion that would never require implementation of the contingency taxes. This high economic growth path reflects the assumption that real GNP increases 1 1/3 percentage points faster per year than under the official forecast, starting with fiscal year 1983. Such a growth assumption is not unrealistic.

The contingency tax plan would have only two provisions, each raising about half the required revenue. The first provision would be an across-the-board tax on individuals and corporations equivalent to a 5 percent surcharge on taxes otherwise due. The other provision would be an excise tax on domestically produced and imported oil of $5 per barrel. In order not to give an unintended price advantage to imported refined products, an excise tax equivalent to a $5 per barrel tax on crude oil would be levied also on imported refined products, such as heating oil, diesel fuel, gasoline and jet fuel. Both provisions of the plan would be temporary taxes, staying in place for no more than 36 months.

The contingency tax alternative shown in the budget raises $146 billion over the 36-month period beginning October 1, 1985. These estimates were based upon one of several alternatives under consideration. The specific plan we will be sending to Congress for adoption this year will conform to the general outline I mentioned earlier. Projected revenues from this plan will be in the range of $130-$150 billion over a 36-month period. The exact amount will depend upon the specific details of the structure.

A surcharge on individual income taxes has been selected as one component of the contingency tax plan because it will have a broad impact and will not change the distribution of taxes paid. It would be an across-the-board 5 percent tax increase for everybody. For example, a family of four earning $10,000 would pay a surcharge of $15, or 5 percent of its $291 tax liability. At $50,000 of income, the family of four would pay a surcharge of $358, or 5 percent of the $7,165 in tax it would otherwise owe. At $100,000 of income a family of four would pay a surcharge of about $1,100.

The $5 per barrel oil excise tax has been selected for the other component of the contingency tax plan because it raises the needed revenues in a way that also has a very broad temporary impact on all taxpayers and all sectors of the economy. The increased burden of the oil tax on consumers will be relatively small. The $5 tax on a barrel of oil would translate roughly into a 12 cent increase in the price of a gallon of gasoline and a 12 cent increase in the price of a gallon of home heating oil. Both of these price increases have been more than offset by recent reductions in the world price of oil; and, current actions being contemplated by oil producing countries suggest that prices may be reduced further during the next few years. For a typical car owner who drives 10,000 miles a year, the 12 cent per gallon increase would amount to a $62 annual increase in the cost of gasoline he consumes. For the average home heated by oil, the 12 cent per gallon increase in the cost of home heating oil will mean an increase in fuel costs of about $60 a year.

Also taken into consideration in the selection of an excise tax on oil as one element of the contingency tax plan is the fact that individuals and businesses will be encouraged to conserve on their consumption of oil from whatever level of use would otherwise prevail in 1986-1988. This would be a small but significant step toward further reducing our reliance on uncertain foreign supplies, which could potentially create a national emergency if interrupted.

Relationship to Other Tax Policies

Some may inquire why we are proposing contingency taxes to take effect in the fall of 1985, if needed, when the Economic Recovery Tax Act of 1981 (ERTA) provides a further 10 percent across-the-board individual income tax reduction in July of this year and indexation of the individual income tax structure beginning January 1, 1986. It is a fundamental mistake to consider delay or repeal of the third year of the tax reduction and delay or repeal of indexation as a substitute for the contingency tax plan. Repeal of the third-year tax cut and indexation would have effects entirely different from those of a temporary surcharge.

Economic impact. The individual income tax reductions Congress enacted in 1981 must be retained if we are to correct the serious disincentives to work and save that had been built into the prior tax structure. For the most part these disincentives did not occur by design but simply grew over the years as high rates of inflation pushed taxpayers' incomes into ever higher marginal rate brackets. The across-the-board tax reductions rolled back the steady upward trend of marginal tax rates on labor and savings income and the indexation provision places a halt on this trend for the future.

If we look at the experience of a typical family of four that earned the median income of about $24,300 in 1980, the first two phases of the across-the-board rate reductions enacted under ERTA provide a tax cut in 1983 of $533, but almost 80 percent of that tax cut is lost through bracket creep so that the net tax cut is only $109. The third-year reduction almost triples this net tax cut from $109 to $294. By 1985 this median income family will receive a net tax increase of $101 if the third year reduction and indexing are repealed. If those provisions are retained, however, this tax increase is converted into a net tax cut totaling $399.

Repeal of the remaining tax reductions already in the law would substantially reduce any real tax cut for most taxpayers. Consequently, repeal would also deny much of the incentive required to maintain the noninflationary growth necessary to avoid the contingency taxes. Lower real growth over the next few years would cause high interest rates and higher deficits. Repeal at this time, when the economy is struggling out of the recession, would be particularly senseless and counterproductive.

The contingency surcharge, by contrast is a temporary tax measure that, by design, can only be implemented if the economy is in a period of growth. It will temporarily mitigate, but not permanently eliminate, the tax incentives to work and save now part of the law.

Distributional impact. Even if the economic impact of a temporary surcharge in fiscal year 1986 were identical to the impact of repealing permanent tax cuts this year, the two measures are unlikely substitutes for each other because of the enormous differences in the way they affect taxpayers at different levels of income. Both the third-year of the tax cut and indexation provide the largest percentage reductions in tax at the lowest income levels. Repeal of both those provisions of ERTA would raise taxes 24.3 percent on those earning less than $10,000, as shown on Table 1. For those with incomes between $10,000 and $50,000, tax increases would be a little over 15 percent. At higher income levels this percentage declines sharply. For those earning more than $200,000, repeal would mean a tax hike of only 3.1 percent. This percent is quite low, in large measure, because tax on income in excess of $162,400 on joint returns and $81,800 on single returns is unaffected by the third-year cut. Those with income below $50,000 would pay 72 percent of the tax increase arising from repeal of the third-year cut and 78 percent of the tax increase from repeal of indexation. In contrast, a temporary surcharge would limit large tax increases for lower and middle incomes to 5 percent while raising the tax increase for wealthy taxpayers to 5 percent. The portion of all surcharge revenues raised from those with incomes lower than $50,000 would be reduced from well over 70 percent attributable to repeal to just about 67 percent -- exactly the same fraction of tax currently paid by taxpayers earning less than $50,000.

Responsible budgeting. The three-year phased-in tax reduction put in place in 1981 was proper tax policy to enact at that time and even more necessary a year and a half later, as the economy begins to grow again. The indexing provision enacted in 1981 is not only the proper tax policy to assure strong growth in the future but it is also the linch pin to responsible budgeting. Repeal of the indexing provision of ERTA would permit Congress to finance ever higher levels of government spending without once enacting another tax increase. To many, this is a very tempting prospect because automatic tax increases are easier to accept than explicit ones that must be legislated. This does not mean, however, that they affect taxpayers and taxpayer incentives any differently. If revenue is to be raised, repeal of indexing is the worst alternative because that would foreclose weighing the benefits of future government spending against the burdens of future taxes.

Further, under a non-indexed system, the higher the rate of inflation, the more revenue there will be available. Thus, there would be an incentive for Congress to pursue inflationary policies. For this same reason, the money markets would likely anticipate renewed inflationary policies if indexation is repealed.

This Administration firmly believes in the principle of accountability. There should not be another tax increase without explicit legislation. The legislative process forces tough debate and tough decisions, all subject to review and criticism by affected constituencies. This is the only way responsible budget policy can be formulated.

Another caution is in order. Currently, there is great pressure on Congress to repeal the provisions of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) requiring withholding on dividends and interest. Unfortunately, much of the pressure to repeal withholding comes from persons who misunderstand the impact withholding will achieve. At a time in which we are facing high deficits it would be grossly unfair to repeal these tax provisions. Under withholding, there is no tax increase on honest and careful taxpayers; nearly three-fourths of the revenue increase comes from taxpayers who are not paying the tax that they owe. Repealing withholding would result in a revenue loss of over $18 billion over the next six fiscal years. (This figure excludes the effect of the information reporting provisions of TEFRA. If the information reporting provisions were also repealed the revenue loss would be $23 billion.) We can hardly ask honest taxpayers to pick up this additional burden. Repealing withholding at this time would also send a message that the government does not take seriously the major effort initiated last year to insure better compliance with the tax laws in general.

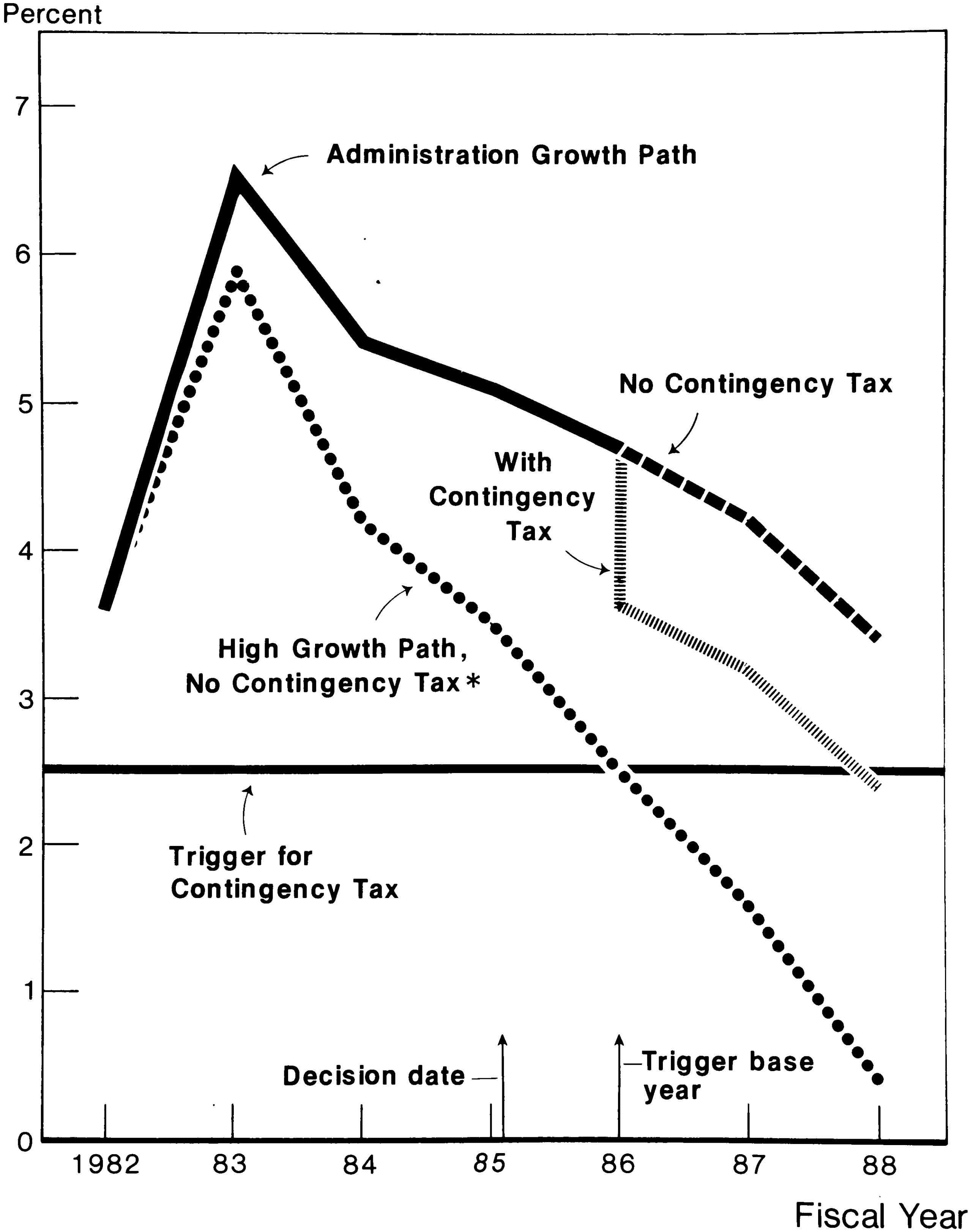
Conclusion

In conclusion, Mr. Chairman, there are probably some sitting on this committee who sincerely believe we will need higher revenues in order to avoid intolerable long-term deficits. There may be others equally convinced that future spending reductions and economic growth will be sufficient to avoid large post-recovery deficits. The Administration is not prepared to guarantee the results of any 2 to 5 year forecast. The art of long-term economic forecasting is not now, and may never be, sufficiently developed to become an exact science: there are simply too many influences that cannot be predicted. Nor is the Administration prepared to second-guess future Congressional action on spending reductions. It is precisely because of these uncertainties that it is imperative to have the insurance that our contingency tax plan will provide. It should satisfy the concerns of those who are certain we will need revenue increases, those who are convinced that we won't, and those, like myself, who are candidly uncertain about our future revenue needs.

Reversing tax reductions already in the Code is not a substitute for contingency taxes. The former are permanent tax reductions designed to provide incentives for the level of growth that is required to avoid large deficits in the future. The contingency tax plan is insurance against uncertainty and unforeseen events that may restrain full recovery. A strong sustained recovery, together with a determined program of restraint on domestic spending, should reduce the deficit without implementation of the contingency taxes. While we hope this occurs, consumers, investors and businesses alike need the assurance that only the contingency tax plan will provide in order for them to make sensible, orderly financial and economic decisions.

Chart 1

THE DEFICIT AS A SHARE OF GNP



*Higher growth than the official path by 1-1/3 percentage point starting fiscal year 1983.

Table 1

The Effect of Repealing the Third Phase of the Tax Reduction and Indexing
Distributed by Adjusted Gross Income Class

(1981 Levels, 1984 Law)

Adjusted gross income class	Tax liability under 1984 law		Change in tax liability due to: Repealing the third phase of the rate reduction			Repealing indexing 1/			Repealing the third phase of the rate reduction and indexing 1/		
	Amount	Percentage distribution	Amount	Percent increase in tax liability	Percentage distribution	Amount	Percent increase in tax liability	Percentage distribution	Amount	Percent increase in tax liability	Percentage distribution
($000)	($millions)	(percent)	($millions)		(percent)	($millions)		(percent)	($millions)		(percent)
Less than 10	$ 4,518	2.1%	$ 628	13.9%	2.6%	$ 424	9.4%	6.5%	$ 1,099	24.3%	3.5%
10 - 15	12,742	5.8	1,372	10.8	5.8	489	3.8	7.4	1,934	15.2	6.2
15 - 20	17,780	8.1	2,018	11.3	8.5	602	3.8	9.2	2,717	15.3	8.8
20 - 30	45,579	20.7	5,489	12.0	23.1	1,458	3.2	22.2	7,115	15.6	22.9
30 - 50	65,901	29.9	7,618	11.6	32.1	2,128	3.2	32.4	10,011	15.2	32.3
50 - 100	39,018	17.7	4,466	11.4	18.8	1,072	2.7	16.3	5,638	14.4	18.2
100 - 200	18,899	8.6	1,706	9.0	7.2	317	1.7	4.8	2,011	10.6	6.5
200 and over	15,619	7.1	420	2.7	1.8	79	0.5	1.2	482	3.1	1.6
Total	$220,057	100.0%	$23,717	10.8%	100.0%	$6,569	3.0%	100.0%	$31,007	14.1%	100.0%

Office of the Secretary of the Treasury
Office of Tax Analysis

March 1, 1983

1/ Assumes 4.5 percent rate of inflation for prior year.

Note: Details may not add to totals due to rounding.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-204

FOR RELEASE UPON DELIVERY
Wednesday, March 2, 1983

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REMARKS BY
DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
GREATER NYC TAKES STOCK IN AMERICA
U.S. SAVINGS BOND COMMITTEE
NEW YORK, N.Y.
MARCH 2, 1983

Good afternoon and thank you for that kind introduction.

I am here on behalf of President Reagan to thank you personally for spearheading the vigorous payroll savings campaigns in your companies. Nineteen Eighty Three is a very upbeat year for Savings Bonds. The new variable, market based rate is the most significant and most exciting change in Savings Bonds in more than 40 years. It marks a dramatic new incentive to save, and ensures a positive competitive rate of return in what has been a stormy savings environment.

Savings Bonds have been an important stabilizing force in our nation's debt-management efforts. We couldn't have done so well in the past without you, and we certainly will need your help in the future.

Since taking on the position as Secretary of the Treasury, I always look forward to speaking events in New York. I worked here for several years. Since leaving, I've learned very quickly that a home is more than just a place to hang one's hat. It is a place where our friends forgive our faults; where our eccentricities are looked upon as evidence of a sturdy character; and our accomplishments are generously magnified. Again, thank you for that kind introduction.

When I look back on the years that I worked in New York, I find it interesting to think how I always thought that the world, more or less, revolved around New York City.

On significant issues like this, I don't like to be proven wrong. However, when I left New York City, I found a group of people who disagreed with me. This group was comprised mostly of a breed called bureaucrats, led by a merry group of warriors called Congressmen, who were convinced that Washington, D.C. was the hub of the world.

This created some confusion. However, after spending a short time in our nation's capitol, I quickly came to my senses. I realize now that if Washington is the hub, then New York is the axle, drive shaft, transmission and engine. So rest assured that I still believe the business and industrial sector is still considered the moving force behind this great nation.

Therefore, as leaders of the business world, you have a great responsiblity. And that is the responsiblity of duty to your employees, to your companies, to your community, to the economy, and to the health of our country.

Thomas Jefferson once said, "Responsiblity and duty is a tremendous engine in a free government." This is as true now as it was in 1791 when Jefferson delivered this message to Congress.

This Administration understands responsibility. It also understands that destiny which results from duty performed may bring anxiety and perils, but seldom failure.

This is what I want to talk about with you today. The duty that we all share in implementing a strategy and program to permanently strengthen our economy and our nation.

You and I both know that a government, like any business, can for a while spend more than it earns. But unlike many Administrations of the past, you and I also understand that a countenance of this bad habit means bankruptcy.

When President Reagan arrived in Washington, it was obvious that the irresponsible spending habits of the past had taken their toll. Twenty-five months ago interest rates were at 21.5 percent. Public spending as a percentage of GNP had reached a postwar high. Taxes had doubled since 1970. Regulation was the master of business and industry, and inflation - public enemy number one - had reached 12.4 percent.

When President Reagan came to office, he shared with the people of this country a desire for a new beginning. He said that the old ways of managing an economy were producing more hardships than happiness. And as an alternative, he offered a program of economic recovery that was based on a belief that this nation's prosperity could be shared by more people in greater quantities. Our program mandated that:

First, irresponsible and inflationary spending habits of the past were to be stopped.

Second, taxation which had suffocated incentive and productivity was to be cut.

Third, the irregular monetary habits of the past were to be replaced by consistent, non-inflationary practices.

And fourth, the regulatory morass which had chained the productive capacities of the private sector were to be cut and disposed of.

In structuring this program, we were guided by our responsibility and duty to the economy and our nation. To that list of driving influences we need to add the term conviction.

History has proven that one thing people cannot permanently resist is the force of great conviction. It was because of the President's conviction of what our economy and nation should be that he was elected. I share with the President his conviction that the plan we have set for economic recovery is the right approach and that our goals and our strategy will not change or be abandoned.

During 1981 and 1982, we implemented significant portions of the President's Economic Recovery Program. We set a foundation for sustainable economic growth. And we've gotten results.

Consider inflation being brought from 12.4 percent to 3.9 percent.

Consider the prime interest rate, slashed from an incredible 21.5 percent in January 1980 to 10.5 percent.

Consider that the out-of-control federal spending rate which was at 17.4 percent in 1980 has been reduced to 10.5 percent this year and with the new budget, to 5.4 percent next year.

And consider an out-of-control income tax burden -- threatening to rise from 13 to 18 percent of personal income between 1980 and 1988 -- now brought under control and held to its historical 12 to 12.5 percent level.

This is progress. But we have achieved these goals because of our unswerving loyalty to economic recovery. And because of our conviction that despite some initial discouragement, our approach was what the people of this nation wanted and deserved.

Those facts provide the foundation for economic progress. Now we see indications that the rest of the house is getting underway. In fact, as indicated by the steady improvements of key economic indicators that usually proceed economic growth, the recovery may be well underway at this time. Encouraging signs include:

The Consumer Price Index increase of 3.9 percent since January 1982, is the smallest 12 month increase in ten years.

Housing starts leaped by 36 percent between December and January to the highest monthly level since September, 1979.

The index of leading indicators was up 3.6 percent in January. It has risen for nine of the last ten months, and now the coincidental indicators are also up -- for January.

Industrial production increased in January by 0.9 percent after a 0.1 percent gain in December.

New orders for durable goods were up a solid 4.5 percent in January, the third consecutive monthly increase.

Businesses trimmed inventories sharply in the final quarter of calendar year 1982. And real inventory liquidation during this period was the largest in any quarter since World War II.

And finally, unemployment dropped in January from 10.8 to 10.4 percent.

The task, however, is not over yet.

Our challenge in the months ahead reminds me of a story about Winston Churchill. During a debate in the British House of Commons, a Parliamentary Member commented on Mr. Churchill's voluminous appetite for spirits, by saying that Mr. Churchill had consumed enough alcohol to fill half of the entire chamber. After the speaker went to his chair, Mr. Churchill proceeded to the podium, looked to the ceiling and said, "Indeed a great accomplishment, but there is so much left to do, with so little time."

In the coming two years, we cannot afford to rest on our achievements. We still have a great deal left to do.

Perhaps the greatest task before us is controlling the growth of federal spending and harnessing the federal deficit. If we allow deficits to grow, we take the chance of draining off a large part of the savings pool, leaving less available for capital formation. Interest rates could remain high and recovery could stall.

This Administration is determined that deficits of such magnitudes will not come to pass. We came to office with a program for boosting private sector investment, and we will not allow ourselves to be diverted from that goal.

This is the objective of the President's deficit reduction program that he proposed during the State Of The Union Address this year. The four basic elements include: a freeze on 1984 spending for COLAs, federal retirement payments, and for a broad range of nonentitlement programs; a program to control the so-called "uncontrollables" better known as entitlement programs; a cutback of $55 billion in defense spending; and, a contingency tax starting October 1, 1985, that would be used only if after implementing the President's spending cuts and freeze, there is still insufficient growth to reduce the deficit below 2 1/2 percent of GNP.

This is a practical cour°se to follow.

As the economy awakens and comes to life, we must continue to put into action our entire program of economic recovery. However, there are certain things we must not do. We must not revert to the overly stimulative monetary and fiscal policies of the past -- for these would surely lead to a resurgence of inflationary pressures and a new round of rising interest rates.

Further, despite some political demands to the contrary, we must not reverse the fundamental tax restructuring put in place in 1981, for these tax improvements provide the non-inflationary incentives to fuel the economic engines of the private sector.

Recently we have heard talk that the Reagan tax cuts are too large and that they should be eliminated. These claims are groundless.

In fact, the tax cuts adopted in 1981 did little more than keep our heads above water. They put a halt to a rapidly increasing tax burden and returned revenues as a percentage of GNP to the levels of the 1960's and 70's.

The second claim we hear is that the tax cuts are unfair and that the third year cut and indexing should be eliminated. This claim is also groundless.

The truth is that all tax rates were reduced by the same amount for all taxpayers. Those who earned between $10,000 and $60,000 dollars -- what is generally defined as the the broad middle class of Americans -- pay about three-quarters of all income taxes. And they receive about three-quarters of the tax cut. Moreover, far too little has been said about the disproportionate benefits to those at the lower end of the income scale as a result of our success in reducing inflation.

Repeal of the third year of the tax cut would strike at the lower and middle income workers and retirees. It would cause a 13.9 percent jump in tax liability for those with less than $10,000 in adjusted gross income, a 12 percent jump for those between $20,000 and $30,000, and only a 2.7 percent jump for those with $200,000 and over.

The repeal of indexing is even more unfair. Without indexing, inflation and social security increases will wipe out the third year cut by 1986 and the entire 23 percent cut by 1987. Indexing is also critical to small businesses. Since 85 percent of small businesses pay taxes through the individual tax rate system, repeal of indexing directly increases taxes and labor costs. Without indexing, only the federal government will benefit from higher inflation by collecting more and more tax dollars as people are pushed into higher tax brackets.

I want to mention one other thing that we must not do. We must not let the international financial system fall to ruin.

Since about the middle of last year, the international monetary system has been confronted with serious financial problems. The debt and liquidity problems of Argentina, Brazil, Mexico and a growing list of other countries have become front page news.

The biggest factors of the international debt crisis are high interest rates and the worldwide recession. These conditions have choked the demand of industrialized nations for imports and, therefore, stifled the ability of developing nations to export. As a result, the debts of many developing countries have become too large for them to handle under present economic circumstances. The international financial and economic system is experiencing strains unprecedented since the postwar era -- strains which threaten the world economic recovery.

The problem is serious but not unmanageable.

The first objective must be to bring some degree of liquidity to the international lending system. The IMF was created in 1944 to assist countries that are experiencing temporary balance of payment problems. If the IMF is to be able to continue in this role, it must have adequate resources to deal with the current situation.

I understand those who ask, "Why bail out the banks and spend more money abroad when we need it at home?"

The reason for concern about the international financial crisis is simple -- exports and jobs.

The United States exports 20 percent of everything it produces. This accounted directly for over 5 million jobs in 1982, including one out of every eight jobs in manufacturing industries. Of even greater importance to revitalizing our economy it was estimated that in the 1970s, four out of every five new jobs in U.S. manufacturing came from foreign trade. On average it is agreed that a $1 billion increase in exports results in 24,000 new jobs.

I am sure you know that the U.S. has agreed to an increase in funding of the IMF of 47 percent. I look at this as an insurance policy against a loss of jobs -- insurance against catastrophic losses.

We cannot afford to lose the exports, the jobs, or the momentum for general economic recovery that is just beginning to take hold. We cannot afford to abandon our friends and our interests overseas, for their sakes and ours.

I began talking about duty. I want to get back to that theme because that is why we are here today.

It is the duty of every American to serve his nation. Your role in supporting U.S. Savings Bonds is a significant contribution that has not gone unrecognized in the Department of the Treasury.

Besides acting as a secure investment for the individual, savings bonds play a key role in our nation's debt servicing. Since 1935, savings bonds have helped reduce the Treasury's need to borrow in the open market, thereby reducing pressures on interest rates from federal borrowing.

When Americans cut back on savings bonds purchases, there is more pressure on the Treasury to borrow from the market. Increased Treasury borrowing, in turn, drains funds that otherwise would be available for capital investment. More participation in the Savings Bonds Program will help get the government out of the market-borrowing business and create more room for economic expansion.

Today, Americans hold more than $68 billion worth of savings bonds. That is $68 billion that the government does not have to borrow in the open market. That permits new savings that the private sector can pour into new ideas, new products, and new jobs that will lead the nation into a future that is bright and prosperous.

Savings bonds play an important role in our economy, and here is where your role comes into play. Some 80 percent of all savings bonds are through the payroll savings plan. The plan has prospered though the support of thousands of business leaders, like you, who promote and operate payroll savings plans. The result has been the enthusiastic participation of employees who find it the one sure way to accumulate reserves for their future.

With $4 of every $5 dollars in savings bonds coming through payroll savings, the plan has spearheaded the bond program's tremendous contribution to the American economy.

Offering payroll savings in your companies, and volunteering to convince other business leaders to do the same, is the key to a successful bond program. And this shouldn't be hard. Between the last quarter of 1982, savings bonds sales were up 19 percent over the year before, and in January were up 23 percent.

The rush to buy bonds makes sense. How else can an individual better earn market-based rates, currently at over 11 percent for savings bonds, for as little as $25? For that amount of money, the saver also gets a guaranteed minimum return of 7 1/2 percent. The investment is free from state and local income tax. The principal and interest are guaranteed safe, and it is a great investment in the future of this nation.

The new variable rate on savings bonds makes this investment instrument competitive in the big leagues of the investment world. It further plays an important part in ensuring that we do not finance our government's needs, at the expense of investment and growth, in the private market. So you, who are the the business leaders of our nation, have a key role to play in helping to keep interest rates declining and, thereby, promoting the economic recovery.

In closing, I want to refer to a statement made by President Woodrow Wilson that sums up my feelings about the potential of America. "Great achievements are the product of great people. They are the result of many generations of effort, toil, and discipline. They do not stand by themselves; they are more than individual. They are the incarnation of the spirit of a people."

The success of our economic recovery, and ultimately our nation, depends on great achievements and great people. We have in this country the resources to make our economic system work, and with the right measures of duty and conviction we will ensure that it does.

Thank you.

***

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE March 2, 1983

RESULTS OF TREASURY'S AUCTION OF 45-DAY CASH MANAGEMENT BILLS

Tenders for $9,004 million of 45-day Treasury bills to be issued on March 7, 1983, and to mature April 21, 1983, were accepted at the Federal Reserve Banks today. The details are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:

	Price	Discount Rate	Investment Rate (Equivalent Coupon-Issue Yield)
High -	98.988	8.096%	8.32%
Low -	98.981	8.152%	8.37%
Average -	98.984	8.128%	8.35%

Tenders at the low price were allotted 20%.

TOTAL TENDERS RECEIVED AND ACCEPTED BY
FEDERAL RESERVE DISTRICTS.
(In Thousands)

Location	Received	Accepted
Boston	$ 120,000	$ 44,000
New York	28,628,000	8,564,000
Philadelphia	--	--
Cleveland	115,000	10,000
Richmond	9,000	200
Atlanta	9,000	--
Chicago	1,702,000	66,000
St. Louis	10,000	--
Minneapolis	50,000	--
Kansas City	20,000	10,000
Dallas	--	--
San Francisco	2,860,000	310,000
TOTALS	$33,523,000	$9,004,200

R-2063

THE SECRETARY OF THE TREASURY
WASHINGTON 20220

March 2, 1983

Dear Mr. Chairman:

The purpose of this letter is to respond to the questions raised during my appearance before the Committee on February 3 concerning the revenue estimate for interest and dividend withholding and the current level of under-reporting of interest and dividend income.

The revenue estimate for withholding was derived in the following manner:

The base for the estimate is the amount of unreported interest and dividend income. Excluded from this base (throughout this letter) are interest and dividend payments that are not affected by the withholding rules, such as interest paid by individuals. Based on the Internal Revenue Service's research programs, including the Taxpayer Compliance Measurement Program, it is estimated that, at 1983 levels, $25 billion of interest and dividend income that should be reported on tax returns will not be reported in the absence of the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA).

We wish to make clear that this estimate of the interest and dividend tax gap is based upon conservative assumptions. An estimate based on all payments of interest and dividends and on claimed deductions of interest (the National Income Accounts analysis) by the Bureau of Economic Analysis of the Department of Commerce concludes that the tax gap of unreported interest and dividends is almost twice as large as that estimated by the Treasury Department. We believe, however, that the absence of certainty as to the cause of this discrepancy requires the use of the more conservative estimate of the size of the gap of unreported interest and dividends, rather than the much larger number indicated by the National Income Accounts, or an average of the two numbers.

Approximately 86 percent of all interest and dividend payments -- including most interest paid by banks and thrift institutions -- were subject to information reporting prior to enactment of TEFRA. As mentioned above and based on the conservative estimating techniques also noted above, the amount of interest and dividend income earned but not reported prior to TEFRA was $25 billion (interest earned but not reported was about $18 billion and unreported dividend income was about $6.5 billion).

For interest payments on bearer obligations and on most Federal obligations, there was no information reporting required prior to TEFRA. For payments not subject to information reporting, the rate of compliance was only about 78 percent. Thus, in the absence of any of the TEFRA provisions 22 percent ($7 billion) of interest on obligations not subject to information reporting would go unreported by taxpayers. Because the amount of payments not subject to information reporting was small compared to the amount of payments for which information reports were required to be filed, the combined rate of compliance for all interest and dividends without the TEFRA provisions is estimated to be about 90 percent, leaving the total gap of $25 billion mentioned above.

A comprehensive system of information reporting will increase the rate of compliance on all payments to 91 percent. Thus, the broadened information reporting introduced by TEFRA will, by itself, only reduce the amount of unreported interest and dividends to $21 billion, still an unacceptable gap.

The withholding provisions in TEFRA reduce the revenue loss from the $21 billion that goes unreported even after the broadened information reporting in TEFRA. The 10 percent withholding on that amount improves compliance by $2.1 billion of additional tax collections at 1983 levels, even if withholding causes no further increase in reporting. (The total revenues raised through 1988 from the improved compliance due to withholding is $13.1 billion.) In fact, compliance will increase more than this amount because some persons who do not now report receipts of interest and dividends (and who would not report such receipts even under the expanded information reporting provided by TEFRA) will be inclined to report and pay tax on the entire payment once such payments are subject to withholding. The amount of induced compliance resulting from this tendency again was conservatively estimated.

It is useful to compare the above figures on noncompliance and unpaid taxes on interest and dividend income with corresponding experience with respect to wages subject to withholding. Not only is the compliance rate on wages significantly higher than that on interest and dividends, but even when wage income is not reported on tax returns, taxes are collected through the existing withholding system. As a result essentially 100 percent of taxes due on wages subject to withholding are collected.

With respect to payments that are currently reported by taxpayers, the new withholding provision will raise a small amount of revenue -- about $0.3 billion -- generated on an annual basis because of an acceleration of tax collections. In addition, in the period immediately after withholding becomes effective, there will be a one-time acceleration of receipts of $3.9 billion. This is because no credits from prior year withholding will offset current withholding receipts in the first year. This acceleration of tax payments required by withholding will treat taxes due on interest and dividends essentially like taxes due on wages. Taxes on all these sources of income will be paid on a timely and fair basis, as the income is earned.

The enclosed table shows the breakout of the three components of the withholding revenue estimate: increased compliance resulting from expanded information reporting, increased compliance from the imposition of withholding, and the acceleration or speedup of tax payments.

I would like also to correct any misleading impression that may have arisen from a 1981 study undertaken by the Internal Revenue Service. Some persons have asserted that this study found a 97 percent rate of compliance for all dividends and interest. That is incorrect. This study was not designed to measure the level of interest and dividend compliance generally. Rather, the study focused on certain limited situations that are not at all representative of the overall compliance problem. Specifically, the study measured noncompliance only in cases meeting each of the following three conditions:

(i) the taxpayer had filed a proper tax return,

(ii) the payor had filed an information return (Form 1099), and

(iii) the information return was readable and contained a proper taxpayer identification number.

Unfortunately, one or more of these conditions are not met in a great many situations. Many taxpayers who should file tax returns do not. Currently, between 5 and 6 million taxpayers fail to file required tax returns. In addition, over 11 percent of information returns for interest and dividends lack a taxpayer identification number, or show an improper number. For taxpayers who file income tax returns on a timely basis, and provide payors with information that enables them to file a proper Form 1099, it is not surprising that voluntary compliance is at a materially higher level than occurs in situations where either a tax return is not properly filed or accurate information is not provided to the payor. As reported above, it is estimated that prior to TEFRA the rate of taxpayer compliance for interest and dividend income of all taxpayers is 90 percent, based on conservative assumptions.

Many have suggested that the compliance levels sought through interest and dividend withholding could be achieved by a vastly enlarged IRS audit program. This is simply not a realistic proposal. An attempt to achieve the compliance levels that will be obtained under withholding would require literally millions of new taxpayer contacts, audits, and legal proceedings. Consequently, attempts to resolve the compliance problem through a stepped-up audit program would be perceived correctly as harrassment. This would seriously damage ongoing efforts to insure honest taxpayers that our tax system is fair and uniformly applied in such a way as to encourage the highest degree of voluntary compliance with the law.

Sincerely,

Donald T. Regan

Donald T. Regan

The Honorable
Robert Dole
Chairman, Senate Finance Committee
Washington, D. C. 20510

Revenue Effect of Withholding on Interest and Dividends
(Including Expanded Information Reporting)

($ billions)

	Fiscal Years 1983	1984	1985	1986	1987	1988	Cumulative total (1983-1988)
Reporting (compliance)	0.1	0.4	0.7	0.9	1.2	1.3	4.6
Withholding:							
Interest:							
Speedup	0.7	1.9	0.2	0.2	0.2	0.2	3.4
Compliance	0.2	1.6	1.7	1.7	1.8	1.9	9.0
Total interest	0.9	3.5	1.9	1.9	2.0	2.2	12.4
Dividends:							
Speedup	0.2	1.1	0.1	0.1	0.1	0.1	1.7
Compliance	0.1	0.7	0.8	0.8	0.9	0.9	4.1
Total dividends	0.2	1.8	0.8	0.9	1.0	1.1	5.8
Total:							
Speedup	0.9	3.0	0.3	0.2	0.3	0.4	5.1
Compliance	0.3	2.3	2.4	2.5	2.7	2.9	13.1
Total withholding	1.1	5.3	2.7	2.8	3.0	3.2	18.2
Grand total:							
Speedup	0.9	3.0	0.3	0.2	0.3	0.4	5.1
Compliance	0.4	2.7	3.1	3.5	3.8	4.2	17.7
Total	1.2	5.7	3.4	3.7	4.2	4.5	22.7

Office of the Secretary of the Treasury
Office of Tax Analysis

March 1, 1983

Note: Details may not add to totals due to rounding.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
MARCH 3, 1983

CONTACT: Robert Don Levine
566-2041

TREASURY BULLETIN GOES QUARTERLY

The winter (February 1983) Treasury bulletin came off the presses today redesigned as a quarterly. Extensive changes in content from the former monthly format aim at cutting production costs while continuing to make available in a more compact and usable form information gathered by the Treasury Department.

Excessive detail and data available from other published sources have been eliminated from the statistical tables. The Bulletin, much streamlined as a result, continues to provide its users with vital information, principally in summary form.

Secretary of the Treasury Donald T. Regan says in an introduction to the new Bullletin "We view the changes as constructive ones that will strengthen the Bulletin as an informative and timely publication."

The new quarterly Treasury bulletin is divided into four major sections: financial operations, international statistics, cash management/debt collection, and special reports. The first section incorporates tables relating to federal fiscal operations, federal obligations, the federal debt and financial operations of government agencies and funds. The second brings together international financial statistics and information on capital movements and foreign currency positions. Statistics on receivables due from the public, reflecting the major governmental debt collection effort, are included in the third. Finally, the fourth section is comprised of miscellaneous reports.

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R-2064

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

3-2-83

FOR RELEASE AT 12:00 NOON

STATEMENT OF THE HONORABLE BERYL W. SPRINKEL
UNDER SECRETARY OF THE TREASURY
FOR MONETARY AFFAIRS
BEFORE THE
HERITAGE FOUNDATION/PHILADELPHIA SOCIETY
CONFERENCE IN MEMORY OF WILSON E. SCHMIDT
Washington, D.C.
March 3, 1983

Solving International Credit Problems

Wil Schmidt was a close and long-time friend. We served together on the Shadow Open Market Committee, which benefitted from his insightful international monetary analysis. During his brief tenure as nominee for Executive Director to the World Bank, he contributed the major intellectual input to our Multilateral Development Bank Assessment, and was therefore indirectly reponsible for the shift toward a market-oriented development policy which is a hallmark of the Reagan Administration. I am grateful for the knowledge he imparted to me and others, and I miss his friendly, competent, and honest counsel. I am honored to participate in this conference dedicated to his memory.

Since the middle of last year the international financial system has been confronted with serious strains, as a number of major borrowers experienced difficulty servicing their external debt. I would like to outline my view of the dimensions of the current problem, the potential dangers it poses, and the measures which have been or are being taken to see us through.

Defining the Problem

Over the past year Argentina, Brazil, Mexico, and a growing list of other countries have been finding their foreign debt burdens too large to manage. International lenders have become pessimistic about prospects for these countries, which are largely middle or upper-income developing nations, and have been pulling back sharply from further lending to them. The resulting strains on the international financial system threaten to derail world economic recovery -- and if handled badly could fundamentally disrupt the international monetary system.

In the well-publicized cases of Argentina, Mexico, and Brazil, the lending exposure of banks is so large that the liquidity problems of borrowers have led to some market speculation that the solvency of lenders in turn might be in jeopardy. As of mid-1982, these three countries owed $145 billion to foreign banks, and the share of U.S. banks in that total was about $55 billion. While the danger to U.S. banks has been overstated in some cases, many banks have become more cautious in their lending as a result of this experience. This may be a positive sign for the longer run, but under present circumstances there is a danger that the banks could go too far, thereby compounding existing debt problems and driving other countries which are now in reasonably good shape into financial difficulties.

This situation didn't develop overnight, but over a period of years. And the key players were not just a few big banks and undisciplined borrowers, but people and governments everywhere.

The essence of the problem has been an unwillingness to accept the fact that there are finite limits to how fast an economy can grow, and how fast the standards of living of its citizens can improve without significant policy changes. Our governments acted as if there were, in fact, such a thing as a free lunch. Thus, in the 1960s and 1970s economic policy in virtually all countries became more and more inflationary. Monetary and fiscal discipline were abandoned in the search for faster growth -- but in the end we found that inflationary policies weren't buying us higher real growth. There was some short-term stimulus at times, but in the longer run investment and productivity were declining, both inflation and unemployment were rising, and longer-term growth prospects were deteriorating. For developing countries, where there was an obvious need for major improvements in standards of living, there was also an irresistible temptation to push development plans too far, too fast with inappropriate economic policies. In both developed and developing countries, the resulting inflationary psychology depressed saving and increased borrowing. Supply side incentives were frequently suppressed.

On top of this came the oil shocks. These further stimulated inflation in the short run, and at the same time created a need for further major structural adjustments in oil-importing economies. In most of our countries, the necessary structural adjustment was not allowed to occur, but was instead impeded by controls, subsidies, and inflationary economic policies. One counterpart of this failure to adjust was the persistence of unprecedentedly large current account deficits and foreign borrowing requirements in the oil-importing countries, especially developing countries. Some oil-exporting countries also borrowed heavily abroad, relying on increasing future oil revenues to finance ambitious development schemes. Most of this borrowing was provided by commercial banks in industrial countries like the United States.

By the middle of 1982, the total debt of non-OPEC developing countries was over $500 billion -- roughly five times the level of their debt in 1973. Net new borrowing by these countries from commercial banks in the major industrialized countries rose to $37 billion in 1979, $43 billion in 1980, and $47 billion in 1981. By the middle of 1982, the stock of debt owed to the private Western banks by non-OPEC developing countries totaled around $270 billion, of which more than half was owed by just three countries in Latin America -- Argentina, Brazil, and Mexico.

Over the last two years, there has been a pronounced shift to non-inflationary policies in most industrial countries, and this shift has had a major impact. Markets are beginning to recognize that the world economy is now in a disinflationary period, and that this disinflation is going to last a while longer. Inflation expectations which became so entrenched in the 1970s are changing dramatically, and lenders are re-evaluating loan portfolios that they established in a quite different economic environment. Levels of debt which were once expected to decline in real terms (and therefore to remain easy for borrowers to manage, relative to growing export receipts under conditions of high inflation) are now seen to be high in real terms and not so manageable in a world of weak export prices and slow economic growth. Banks have become more cautious on all their lending -- not just to developing country governments but to domestic corporations as well.

In the resulting credit squeeze many international borrowers are finding it more difficult, and more costly, to obtain new loans. And as some borrowers are late in meeting payments, or reschedule their debts, lenders in turn face a squeeze on current earnings from problem loans.

Importance of an Orderly Resolution

If that were the entire substance of the international debt problem, it would be difficult for governments or the public to worry very much. Why should we be concerned if some foreign borrowers get cut off from bank loans? And why worry if banks lose some money? Nobody forced them to make those loans, and it is reasonable to expect them to live with the consequences of their own decisions like any other business. If all the U.S. government had in mind was throwing money at the borrowers and their lenders, it would be difficult to justify spending the taxpayer's money on any efforts to resolve the debt crisis, especially at a time when we are cutting back so much on domestic spending.

But of course, there is more to the problem -- and to the solution. There is the potential that, if the situation were handled badly, the difficulties facing LDC borrowers might come to appear so hopeless that they would be tempted to take abrupt and destabilizing measures. The present situation is manageable, but billions of dollars in simultaneous loan losses would pose a threat to the basic soundness of the international financial system, and to the American financial system as well. Such an outcome would have profound consequences for growth and employment in both the industrialized countries whose banks do most of the lending, and in the borrowing countries.

For the United States, there are both direct and indirect effects. As a general matter, the economic health of LDC borrowers is important to U.S. exporters, farmers, and investors as well as to the banking system. There are downside risks for the U.S. growth and employment outlook, associated with the debt problem. And a squeeze on bank earnings and capital positions could mushroom into a significant reduction in banks' ability to lend to domestic customers.

Last year, new lending to non-OPEC developing countries dropped by roughly half, to something in the range of $20 to $25 billion. Some of this reduction was probably intended by the borrowers themselves, as their past adjustment efforts reduced their external borrowing requirements. But the cutback in new lending has gone far beyond that point, and has been forcing developing countries to cut back their trade and current account deficits sharply to match the reduced amount they can now borrow.

The only quick way for these countries to significantly reduce trade and current account deficits is to cut imports, either by depressing their economies or by restricting imports directly through tariffs and quotas. Both of these are painful to the borrowing countries and difficult to sell politically to their citizens. And they are also painful for the United States economy, because a very large part of the reduction in LDC imports -- about one-third -- comes at the direct expense of our exports.

International trade is tremendously important to the United States. Trade was the fastest-growing part of the world economy in the last decade -- but export volume grew even faster in the United States in the last part of that decade, more than twice as fast as the volume of total world exports. Exports of goods and services as a share of U.S. gross national product doubled between 1970 and 1979, and now account for about 12 percent of GNP. By the end of the decade, one out of every three acres of U.S. agricultural land was devoted to production for export. In manufacturing, one out of every eight jobs produced for export, and nearly 20 percent of our total manufactured goods output was exported. But of our total exports, nearly 30 percent goes to non-OPEC developing countries -- thus, all that U.S. production and all those U.S. jobs are very vulnerable to sharp cutbacks in their imports.

This adjustment would, at minimum, become much more painful for both the borrowing countries, and for lending countries like the United States, if banks were to pull back <u>entirely</u> from <u>new</u> lending. This would require borrowers to make yet another $20 to $25 billion cut in their trade and current account deficits, which would be considerably harder to manage if it came right on the heels of the cuts they have already made. At minimum this would result in painful export losses for the United States and other industrial countries which could threaten our recovery.

There is certainly nothing wrong with greater exercise of prudence and caution on the part of commercial banks -- far from it. Since banks have to live with the consequences of their decisions, sound lending judgment is crucial. In addition, greater scrutiny by lenders puts pressure on borrowers to improve their capacity to repay, and creates an additional incentive for borrowing countries to undertake needed adjustment measures.

But a serious short-run problem has arisen as a result of the size of the debt of several key countries, the turn in the world economic environment, inadequacy of adjustment policies, and the speed with which countries' access to external financing has been cut back.

The question is one of the speed and degree of adjustment. While the developing countries must adjust their economies to reduce the pace of external borrowing and maintain their capacity to service debt, there <u>is</u> a limit, in both economic and political terms, to the speed with which major adjustments can be made. Effective and orderly adjustment takes time, and attempts to push it too rapidly can be destabilizing.

The greater threat to the economic and financial system stems from the fact that borrowing countries have already taken such difficult adjustment measures to get this far that if they were forced to contemplate a second year of massive cutbacks in available financing, they would be strongly tempted to use other measures to reduce the burden of their debts -- measures which would result in widespread banking loan losses.

When interest payments are more than 90 days late, not only are bank profits reduced by the lost interest income, but they may also have to begin setting aside precautionary reserves to cover potential loan losses. If the situation persisted long enough, the capital of the banks would be reduced.

Banks are required to maintain an adequate ratio between their underlying capital and their assets -- which consist mainly of loans. For some, shrinkage of their capital base would force them to cut back on their assets -- meaning their outstanding loans -- or at least on the growth of their assets -- meaning their new lending. Banks would thus be forced to make fewer loans to all borrowers, domestic and foreign, and they would also be unable to make as many investments in securities such as municipal bonds. Reduced access to bank financing would thus force a cutback in the expenditures which private corporations and local governments can make -- and it would also put upward pressure on interest rates. The more abruptly new lending to troubled borrowing countries is cut back, the more likely it is that the fallout from their problems will feed back on the U.S. financial system and weaken our economy.

Resolving the Debt Problem

There are many major players in this drama -- governments in developing countries, industrial country governments, commercial banks, and private firms and citizens -- and all stand to lose if this situation is not properly resolved. Thus, all should, and indeed must, play important parts in solving the problem. The solution we have been working on has five major elements:

o Economic Adjustment

First, and in the long run most important, must be effective adjustment in borrowing countries. The object is not just to reduce external borrowing requirements, but also to get sound policies in place which lead to a higher economic growth rate and a greater ability to pay for imports in the long run.

Each of these countries is in a different situation, and each faces its own unique constraints. But as a general matter, because there are inherent limits to how much it is possible to depress their economies and cut back their imports, orderly and effective adjustment cannot occur overnight. The adjustment will have to come more slowly, and must involve expanding their exports as well as cutting imports. Thus, it will entail a multi-year effort in most countries, involving measures to address such problems as: rigid exchange rates, subsidies and protectionism, distorted prices, inefficient state enterprises, uncontrolled government expenditures and large fiscal deficits, excessive and inflationary money growth, and interest rate controls which discourage private savings and distort investment patterns.

o The Role of the IMF

The second element in our overall strategy is the continued availability of official financing balance of payments financing from the IMF, on a scale sufficient to see troubled borrowers through the adjustment process. The IMF has a key role because it not only provides temporary balance of payments financing, but also ensures that disbursement of those funds is tied to the condition that borrowers take appropriate policy measures which lead to adjustment. It is this aspect -- IMF conditionality -- which makes the IMF's role in resolving the current debt situation so important.

While it is difficult to judge the adequacy of IMF resources in precise terms, most factors point in the same direction at present. The resources now effectively available to the IMF have fallen to very low levels in absolute terms, in relation to broad economic aggregates such as world trade, and in relation to actual and potential use of the IMF.

At the beginning of this year, the IMF had about SDR 28 billion available for lending. However, SDR 19 billion of that total had already been committed under existing IMF programs or was expected to be committed shortly to programs already negotiated, leaving only about SDR 9 billion available for new commitments. Given the scope of today's financing problems, requests for IMF programs by many more countries must be anticipated over the next year, and it is probable that unless action is taken to increase IMF resources its ability to commit funds to future adjustment programs will be exhausted by late 1983 or early 1984.

We recently concluded negotiations which have been underway in the IMF since early 1981 on a further increase in IMF quotas, the permanent resource base of the Fund. At the outset of those negotiations, many IMF member countries favored a doubling or tripling of quotas, arguing both that large payments imbalances were likely to continue and that the IMF should play a larger intermediary role in financing them. While agreeing that quotas should be adequate to meet prospective needs for temporary financing, the United States felt that effective stabilization and adjustment measures should lead to a moderation of payments imbalances. We also felt that the IMF should have the ability to respond to extraordinary situations for which its ordinary resources would be inadequate, but that a massive quota increase would be an inefficient means of accomplishing this.

Accordingly, the United States proposed a dual approach to strengthening IMF resources, which was adopted by the IMF membership in agreements over the last two months:

-- First, a quota increase which, while smaller than many others had wanted, would enable the IMF to meet members' needs in normal circumstances. The agreed increase in IMF quotas as is 47 percent, an increase from SDR 61 billion to SDR 90 billion (in current dollar terms, an increase from $67 billion to $99 billion). The proposed increase in the U.S. quota is SDR 5.3 billion ($5.8 billion at current exchange rates) representing 18 percent of the total increase. This would leave us with a quota share of just over 19 percent.

-- Our second proposal was the establishment of a contingency borrowing arrangement that would be available to the IMF on a stand-by basis for use in situations threatening the stability of the system as a whole. The Group of Ten, working with the IMF Executive Board, has altered the IMF's General Arrangements to Borrow for this purpose. The GAB is to be expanded from the equivalent of about SDR 6.5 billion at present to a new total of SDR 17 billion, and the GAB will be usable, under certain circumstances, to finance drawings on the IMF by any member country. Under this agreement, the U.S.

commitment to the GAB would rise from $2 billion to SDR 4.25 billion, equivalent to an increase of roughly $2.7 billion at current exchange rates.

We believe this expansion and revision of the GAB offers several important attractions and, as a supplement to the IMF's quotas, greatly strengthens the IMF's role as a backstop to the system:

-- First, since GAB credit lines come primarily from countries that have relatively strong reserve and balance of payments positions, they can be expected to provide more effectively usable resources than a quota increase of comparable size.

-- Second, since the GAB will not be drawn upon in normal circumstances, this source of financing will be conserved for emergency situations. By demonstrating that the IMF is positioned to deal with severe systemic threats, an expanded GAB can provide the confidence to private markets that is needed to ensure that capital continues to flow, thus reducing the risk that the problems of one country will affect others.

-- And third, creditors under this arrangement will have to concur in decisions on its activation, ensuring that it will be used only in cases of systemic need and in support of effective adjustment efforts by borrowing countries.

We believe these steps to strengthen the IMF, if enacted, will safeguard the IMF's ability to respond effectively to current financial problems. Given the financing needs we foresee, we feel it is important that the increases be implemented by the end of this year. Without such a timely and adequate increase in IMF resources, the ability of the monetary system to weather debt and liquidity problems will be impaired, at substantial direct and indirect cost to the United States.

o <u>"Bridge" Financing</u>

However, it takes time for borrowers to design and negotiate lending programs with the IMF and financing arrangements with other creditors. The debt problems of troubled borrowers are sometimes too immediate to wait for that process to reach its conclusion -- in fact, the real liquidity crunch came in the Mexican and Brazilian cases before such negotiations even started.

Thus, the third element in our strategy is the willingness of governments and central banks in lending countries to act quickly to provide immediate and substantial short-term financing packages -- on a selective basis, where system-wide dangers are present -- to tide countries through their negotiations. We have been doing this through arrangements among Finance Ministries and Central Banks, often in cooperation with the Bank for International Settlements. But it must be emphasized that these lending packages are short-term in nature, designed to last for only a year at most and normally much less, and simply cannot substitute for IMF resources which are designed to help countries through a multi-year adjustment process.

o <u>Commercial Bank Lending</u>

In fact, IMF resources in turn have only a transitional and supporting role. The overall amount of Fund resources, while substantial, is limited and not in any event adequate to finance all the needs of the LDCs. While we feel that a sizeable increase in IMF resources is essential, this increase is not a substitute for lending by commercial banks. Bank lending has been the largest single source of LDC financing in the past, and this will have to be the case in the future as well.

Thus, the fourth essential element in resolving debt problems is continued commercial bank lending to developing countries which are pursuing sound adjustment programs. In the last months of 1982 some banks, both in United States and abroad, sought to limit or reduce outstanding loans to troubled LDC borrowers. But an orderly resolution of the present situation requires <u>increases</u> in net lending to developing countries, including the most troubled borrowers, to support effective, non-disruptive adjustment. The increase needed for just three countries -- Brazil, Argentina, and Mexico -- will exceed $10 billion in 1983, and it now appears that that financing will be available.

- <u>Sustainable Growth and Free Trade</u>

The final part of our strategy is sustainable economic growth and maintenance of a free trading system. The world economy is poised for a sustained recovery: inflation rates in most major countries have receded; nominal interest rates have fallen sharply; inventory rundowns are largely complete. Solid, observable U.S. recovery has been one critical ingredient missing for world economic expansion. We believe this is now getting underway, as evidenced by the recent drop in unemployment and upturns in production. Establishing credible growth in the other industrial economies is also important, and we believe the basis is being laid in most of those countries as well.

However, both we and they must exercise caution at this turning point. Governments must not give in to political pressures to stimulate their economies too much through excessive monetary or fiscal expansion. A major shift at this stage could place upward pressure on inflation and interest rates.

In addition, rising protectionist pressures, both in the United States and elsewhere, pose a real threat to global recovery and to the resolution of the debt problem. Protectionist measures bring retaliation, and everybody loses as a result. More importantly for the debt problems, we must remember that export expansion by the developing countries is crucial to their balance of payments adjustment efforts. Protectionism in the United States and other industrial countries cuts off the major channel of such expansion. That adjustment is essential to restoring developing country debtors to sustainable balance of payments positions and avoiding further liquidity crises -- and as we have seen, it is therefore essential to the economic and financial health of the United States.

The only solution is a stronger effort to resist protectionism. As the world's largest trading nation, the United States carries a major responsibility to lead the world away from a possible trade war. The clearest and strongest signal for other countries would be for the United States to renounce protectionist pressures at home and to preserve its essentially free trade policies.

The Oil Market Situation

While it was clearly not a part of our strategy for resolving the debt problem, the timing of the drop in world oil prices is fortuitous. We believe this will be a significant positive factor for world economic recovery.

Some observers have worried about the negative impacts of falling oil prices -- confusion in financial markets, rearrangement of energy investment plans, and strains on some banks heavily involved in energy lending. There are costs of this type in the short run, but they are far outweighed by the gains to both the U.S. and world economy. These gains include stronger growth, higher employment, lower inflation, and improvement in the trade balances of oil-importing countries. While some countries and some firms may incur transitional costs, the winners outnumber the losers.

Conclusion

The international debt problem is a serious one, with potentially severe consequences if it were not handled well. But the problem is manageable, and it is being managed. Much more remains to be done -- by governments, by borrowers, by lenders -- and it would still be possible for the United States in particular to take actions which would make the situation worse.

Our hope is that the United States will instead follow the path toward a successful resolution -- a path of sound monetary and fiscal policies for a sustainable economic recovery, of support for the International Monetary Fund in its crucial role in tiding countries through necessary adjustment periods, of continued willingness to provide private financing to developing countries, and of commitment to a free trading system. Our position as a world leader requires it. Our own self-interest requires it as well.

TREASURY NEWS

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FOR IMMEDIATE RELEASE CONTACT: Marlin Fitzwater
February 22, 1983 202/566-5252

ROGER MEHLE TO RETURN TO PRIVATE SECTOR

Roger Mehle, Assistant Secretary of the Treasury for Domestic Finance, today announced his intention to leave government and return to the private sector. Mehle will remain in his present position while a successor is being selected, but intends to leave in about a month.

Donald T. Regan, Secretary of the Treasury, said, "Roger has produced a significant record of accomplishment. He developed and guided the financing and credit policies of the Federal government in the securities marketplace during a time of unprecedented government borrowing.

"He has helped guide the Depository Institutions Deregulation Committee through a series of actions to increase competition in the financial industry. The Garn-St Germain bill has helped restore the health of the thrift industry. And our proposal for increasing bank powers through holding companies now has widespread industry support. Roger was our point man in all of these achievements."

"I feel we have made important strides in deregulation and modernization of the laws governing financial institutions," Mehle said. "I am proud of our record and this is an appropriate time for me to return to the private sector."

R-2066

TREASURY NEWS

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STATEMENT OF THE HONORABLE DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE
HOUSE BUDGET COMMITTEE
TASK FORCE ON INTERNATIONAL FINANCE AND TRADE
Washington, D.C.
March 7, 1983

The World Financial Situation and the IMF; The Multilateral Development Banks; and The Export-Import Bank

Mr. Chairman and members of the Task Force:

It is a pleasure to appear before you today to explain and support the Administration's proposals for legislation to increase the resources of the International Monetary Fund. At the request of the Task Force, I will also discuss our FY 1984 proposals for the multilateral development banks and the Eximbank.

After extensive consultations and negotiations among IMF members, agreement was completed earlier this month on complementary measures to increase IMF resources: an increase in quotas, the IMF's basic source of financing; and an expansion of the IMF's General Arrangements to Borrow (GAB), for lending to the IMF on a contingency basis, if needed to deal with threats to the international monetary system. These must now be confirmed by member governments, involving Congressional authorization and appropriation in our case, in order to become effective. As background to the legislative proposals which were submitted to the Congress last week, I would like to outline the problems facing the international financial system, the importance to the United States of an orderly resolution of those problems, and the key role the IMF must play in solving them.

The International Financial Problem

Since about the middle of last year, the international monetary system has been confronted with serious financial problems. Last fall the debt and liquidity problems of Argentina, Brazil, Mexico, and a growing list of other borrowers became front-page news -- and correctly so, since management of these problems is critical to our economic interests. The debts of many key countries became too large for them to continue to manage under present policies and world economic circumstances; lenders began to retrench sharply; and the borrowers have since been finding it difficult if not impossible to scrape together the money to meet upcoming debt payments and to pay for essential imports. As a result, the international financial and economic system is experiencing strains that are without precedent in the postwar era and which threaten to derail world economic recovery.

There is a natural tendency under such circumstances for financial contraction and protectionism -- reactions that were the very seeds of the depression of the 1930s. It was in response to those tendencies that the International Monetary Fund was created in the aftermath of World War II, largely at the initiative of the United States, to provide a cooperative mechanism and a financial backstop to prevent a recurrence of that slide into depression. If the IMF is to be able to continue in that role, it must have adequate resources.

The current problem did not arise overnight, but rather stems from the economic environment and policies pursued over the last two decades. Inflationary pressures began mounting during the 1960's, and were aggravated by the commodity boom of the early 1970's and the two oil shocks that followed. For most industrialized countries, the oil shocks led to a surge of imported inflation, worsening the already growing inflationary pressures; to large transfers of real income and wealth to oil exporting countries; and to deterioration of current account balances. For the oil-importing less developed countries -- the LDCs -- this same process was further compounded by their loss of export earnings when the commodity boom ended.

Rather than allowing their economies to adjust to the oil shocks, most governments tried to maintain real incomes through stimulative economic policies, and to protect jobs in uncompetitive industries through controls and subsidies. Inflationary policies did bring a short-run boost to real growth at times, but in the longer run they led to higher inflation, declining investment and productivity, and worsening prospects for real growth and employment.

Similarly, while these policies delayed economic adjustment somewhat, they could not put it off forever. In the meanwhile, the size of the adjustment needed was getting larger. Important regions remained dependent on industries whose competitive position was declining; inflation rates and budget deficits soared; and -- most pertinent to today's financial problems -- many oil importing countries experienced persistent, large current account deficits and unprecedented external borrowing requirements. Some oil-exporting countries also borrowed heavily abroad, in effect relying on increasing future oil revenues to finance ambitious development plans.

In the inflationary environment of the 1970's, it was fairly easy for most nations to borrow abroad, even in such large amounts, and their debts accumulated rapidly. Most of the increased foreign debt reflected borrowing from commercial banks in industrial countries. By mid-1982, the total foreign debt of non-OPEC developing countries was something over $500 billion -- more than five times the level of 1973. Of that total, roughly $270 billion was owed to commercial banks in the industrial countries, and more than half of that was owed by only three Latin American countries -- Argentina, Brazil, and Mexico. New net lending to non-OPEC LDCs by banks in the industrial countries grew at a rising pace -- about $37 billion in 1979, $43 billion in 1980, and $47 billion in 1981 -- with most of the increase continuing to go to Latin America. (See Charts A and B.)

That there has been inadequate adjustment and excessive borrowing has become painfully clear in the current economic environment -- one of stagnating world trade, disinflation, declining commodity prices, and interest rates which are still high by historical standards. Over the past two years, there has been a strong shift to anti-inflationary policies in most industrial countries, and this shift has had a major impact on market attitudes. Market participants are beginning to recognize that our governments intend to keep inflation under control in the future and are adjusting their behavior accordingly.

In most important respects, the impact of this change has been positive. Falling inflation expectations have led to major declines in interest rates. There has been a significant drop in the cost of imported oil. On the financial side, there is a shift toward greater scrutiny of foreign lending which may be positive for the longer run, even though there are short-term strains. Lenders are re-evaluating loan portfolios established under quite different expectations about future inflation. Levels of debt that were once expected to decline in real terms because of continued inflation -- and therefore to remain easy for borrowers to manage out of growing export revenues -- are now seen to be high in real terms and not so manageable in a disinflationary world. As a result, banks have become more cautious in their lending -- not just to LDCs but to domestic borrowers as well.

There is certainly nothing wrong with greater exercise of prudence and caution on the part of commercial banks -- far from it. Since banks have to live with the consequences of their decisions, sound lending judgment is crucial. In addition, greater scrutiny by lenders puts pressure on borrowers to improve their capacity to repay, and creates an additional incentive for borrowing countries to undertake needed adjustment measures.

But a serious short-run problem has arisen as a result of the size of the debt of several key countries, the turn in the world economic environment, inadequacy of adjustment policies, and the speed with which countries' access to external financing has been cut back. Last year, net new bank lending to non-OPEC LDCs dropped by roughly half, to something in the range of $20 to $25 billion for the year as a whole (Chart B), and came to a virtual standstill for a time at mid-year. This forced LDCs to try to cut back their trade and current account deficits sharply to match the reduced amount of available external financing.

The only fast way for these countries to reduce their deficits significantly in the face of an abrupt cutback in financing is to cut imports drastically, either by sharply depressing their economies to reduce demand or by restricting imports directly. Both of these are damaging to the borrowing countries, politically and socially disruptive, and painful to industrial economies like the United States -- because almost all of the reduction in LDC imports must come at the direct expense of exports from industrial countries.

But as the situation has developed in recent months, there has been a danger that lenders might move so far in the direction of caution that they compound the severe adjustment and liquidity problems already faced by major borrowers, and even push other countries which are now in reasonably decent shape into serious financing problems as well.

The question is one of the speed and degree of adjustment. While the developing countries must adjust their economies to reduce the pace of external borrowing and maintain their capacity to service debt, there is a limit, in both economic and political terms, to the speed with which major adjustments can be made. Effective and orderly adjustment takes time, and attempts to push it too rapidly can be destabilizing.

Importance to the United States of an Orderly Resolution

It is right for American citizens to ask why they and their government need be concerned about the international debt problem. Why should we worry if some foreign borrowers get cut off from bank loans? And why should we worry if banks lose money? Nobody forced them to lend, and they should live with the consequences of their own decisions like any other business.

If all the U.S. government had in mind was throwing money at the borrowers and their lenders, it would be difficult to justify using U.S. funds on any efforts to resolve the debt crisis, especially at a time of domestic spending adjustment.

But of course, there is more to the problem, and to the solution. First, a further abrupt and large-scale contraction of LDC imports would do major damage to the U.S. economy. Second, if the situation were handled badly, the difficulties facing LDC borrowers might come to appear so hopeless that they would be tempted to take desperate steps to try to escape. The present situation is manageable. But a downward spiral of world trade and billions of dollars in simultaneous loan losses would pose a fundamental threat to the international economic system, and to the American economy as well.

In order to appreciate fully the potential impact on the U.S. economy of rapid cutbacks in LDC imports, it is useful to look at how important international trade has become to us. Trade was the fastest growing part of the world economy in the last decade -- but the volume of U.S. exports grew even faster in the last part of the 1970's, more than twice as fast as the volume of total world exports. By 1980, nearly 20 percent of total U.S. production of goods was being exported, up from 9 percent in 1970, although the proportion has fallen slightly since then. (Charts C and D.)

Among the most dynamic export sectors for this country are agriculture, services, high technology, crude materials and fuels. American agriculture is heavily export-oriented: one in three acres of U.S. agricultural land, and 40 percent of agricultural production, go to exports. This is one sector in which we run a consistent trade surplus, a surplus that grew from $1.6 billion in 1970 to over $24 billion in 1980. (Chart E.)

Services trade -- for example, shipping, tourism, earnings on foreign direct investment and lending -- is another big U.S. growth area. The U.S. surplus on services trade grew from $3 billion in 1970 to $34 billion in 1980, and has widened further since. (Chart F.) When both goods and services are combined, it is estimated that one-third of U.S. corporate profits derive from international activities.

High technology manufactured goods are a leading edge of the American economy, and not surprisingly net exports of these goods have grown in importance. The surplus in trade in these products rose from $7.6 billion in 1970 to $30 billion in 1980. And even in a sector we do not always think of as dynamic -- crude materials and non-petroleum fuels like coal -- net exports rose six-fold, from $2.4 billion to $14.6 billion over the same period.

Vigorous expansion of our export sectors has become critical to employment in the United States. (Chart G.) The absolute importance of exports is large enough -- they accounted directly for 5 million jobs in 1982, including one out of every eight jobs in manufacturing industry. But export-related jobs have been getting even <u>more</u> important at the margin. A survey in the late 1970s indicated that four out of every five <u>new</u> jobs in U.S. manufacturing was coming from foreign trade; on average, it is estimated that every $1 billion increase in our exports results in 24,000 new jobs. Later I will detail how Mexican debt problems have caused a $10 billion annual-rate drop in our exports to Mexico between the end of 1981 and the end of 1982. By the rule of thumb I just gave, that alone -- if sustained -- would mean the loss of a quarter of a million American jobs.

These figures serve to illustrate the overall importance of exports to the U.S. economy. The story can be taken one step further, to relate it more closely to the present financial situation. Our trading relations with the non-OPEC LDCs have expanded even more rapidly than our overall trade. Our exports to the LDCs, which accounted for about 25 percent of total U.S. exports in 1970, rose to about 29 percent by 1980. (Chart H.) In manufactured goods, which make up two-thirds of our exports, the share going to LDCs rose even more strongly -- from 29 percent to 39 percent.

What these figures mean is that the export sector of our economy -- a leader in creating new jobs -- is tremendously vulnerable to any sharp cutbacks in imports by the non-OPEC LDCs. Yet that is exactly the response to which debt and liquidity problems have been driving them. This is a matter of concern not just to the banking system, but to American workers, farmers, manufacturers and investors as well.

Even on the banking side, there are indirect impacts of concern to all Americans. A squeeze on earnings and capital positions from losses on foreign loans not only would impair banks' ability to finance world trade, but also could ultimately mushroom into a significant reduction in their ability to lend to domestic customers and an increase in the cost of that lending.

Beyond our obvious interest in maintaining world trade and trade finance, there is another less-recognized U.S. financial interest. The U.S. government faces a potential exposure through Federal lending programs administered by Eximbank and the Commodity Credit Corporation. This exposure -- built in support of U.S. export expansion -- amounted to $35 billion at the end of 1982, including $24 billion of direct credits (mostly from Eximbank) and $11 billion of guarantees and insurance. Argentina, Brazil and Mexico are high on the list of borrowers. Should loans extended or guaranteed under these programs sour, the U.S. Treasury -- meaning the U.S. taxpayer -- would be left with the loss. We have a direct interest in avoiding this addition to Federal financing requirements.

All industrial economies, including the American economy, will inevitably bear some of the costs of the balance of payments adjustments LDCs must make and are already making. This adjustment would be much deeper, for both the borrowing countries and for lending countries like the United States, if banks were to pull back <u>entirely</u> from new lending this year. In 1983, for example, a flat standstill would require borrowers to make yet another $20 to $25 billion cut in their trade and current account deficits, which would be considerably harder to manage if it came right on the heels of similar cuts they have already made. Further adjustments are needed -- but again the question is one of the size and speed of adjustment. If these countries were somehow to make adjustments of that size for a second consecutive year, the United States and other industrial countries would then have to suffer large export losses once again. At the early stages of U.S. and world economic recovery we are likely to be in this year, a drop in export production of this size could abort the gradual rebuilding of consumer and investor confidence we need for a sustained recovery.

In fact, many borrowers have already taken very difficult adjustment measures to get this far. If they were forced to contemplate a second year of further massive cutbacks in available financing, they could be driven to consider other measures to reduce the burden of their debts. Here potentially lies a still greater threat to the financial system.

When interest payments are more than 90 days late, not only are bank profits reduced by the lost interest income, but they may also have to begin setting aside precautionary reserves to cover potential loan losses. If the situation persisted long enough, the capital of some banks might be reduced.

Banks are required to maintain an adequate ratio between their underlying capital and their assets -- which consist mainly of loans. For some, shrinkage of their capital base would force them to cut back on their assets -- meaning their outstanding loans -- or at least on the growth of their assets -- meaning their new lending. Banks would thus be forced to make fewer loans to all borrowers, domestic and foreign, and they would also be unable to make as many investments in securities such as municipal bonds. Reduced access to bank financing would thus force a cutback in the expenditures which private corporations and local governments can make -- and it would also put upward pressure on interest rates.

The usual perception of international lending is that it involves only a few large banks in the big cities concentrated in half a dozen states. The facts are quite different. We have reliable information from bank regulatory agencies and Treasury reports identifying nearly 400 banks in 35 states and Puerto Rico that have foreign lending exposures of over $10 million -- and in all likelihood there are hundreds more banks with exposures below that threshold but still big enough to make a significant dent in their capital and their ability to make new loans here at home. Banks in most states are involved, and the more abruptly new lending to troubled borrowing countries is cut back, the more likely it is that the fallout from their problems will feed back back on the U.S. financial system and weaken our economy. Many U.S. corporations also have claims on foreign countries, related to their exports and foreign investments.

Resolving the International Financial Problem

Debt and liquidity problems did not come into being overnight, and a lasting solution will also take some time to put into place. We have been working on a broad-based strategy involving all the key players -- LDC governments, governments in the industrialized countries, commercial banks, and the International Monetary Fund. This strategy has five main parts:

First, and in the long run most important, must be effective adjustment in borrowing countries. In other words, they must take steps to get their economies back on a stable course, and to make sure that imports do not grow faster than their ability to pay for them. Each of these countries is in a different situation, and each faces its own unique constraints. But in general, orderly and effective adjustment will not come overnight. The adjustment will have to come more slowly, and must involve expansion of productive investment and exports. In many cases it will entail multi-year efforts, usually involving measures to address some combination of the following problems: rigid exchange rates; subsidies and protectionism; distorted prices; inefficient state enterprises; uncontrolled government expenditures and large fiscal deficits; excessive and inflationary money growth; and interest rate controls which discourage private savings and distort investment patterns. The need for such corrective policies is recognized, and being acted on, by major borrowers -- with the support and assistance of the IMF.

The second element in our overall strategy is the continued availability of official balance of payments financing, on a scale sufficient to help see troubled borrowers through the adjustment period. The key institution for this purpose is the International Monetary Fund. The IMF not only provides temporary balance of payments financing, but also ensures that use of its funds is tied tightly to implementation of needed policy measures by borrowers.

IMF

It is this aspect -- IMF conditionality -- that makes the role of the IMF in resolving the current debt situation and the adequacy of its resources so important.

IMF resources are derived mainly from members' quota subscriptions, supplemented at times by borrowing from official sources. Assessing the adequacy of these resources over any extended period is extremely difficult and subject to wide margins of error. The potential needs for temporary balance of payments financing depend on a number of variables, including members' current and prospective balance of payments positions, the availability of other sources of financing, the strength of the conditionality associated with the use of IMF resources, and members' willingness and ability to implement the conditions of IMF programs. At the same time, the amount of IMF resources that is effectively available to meet its members' needs at any point in time depends not only on the size of quotas and borrowing arrangements, but also on the currency composition of those resources in relation to balance of payments patterns, and on the amount of members' liquid claims on the IMF which might be drawn. In view of all these variables, assessments of the IMF's "liquidity" -- its ability to meet members' requests for drawings -- can change very quickly.

IMF

Still, as difficult as it is to judge the adequacy of IMF resources in precise terms, most factors point in the same direction at present. The resources now effectively available to the IMF have fallen to very low levels in absolute terms, in relation to broad economic aggregates such as world trade, and in relation to actual and potential use of the IMF.

At the beginning of this year, the IMF had about SDR 28 billion available for lending. However, SDR 19 billion of that total had already been committed under existing IMF programs or was expected to be committed shortly to programs already negotiated, leaving only about SDR 9 billion available for new commitments. Given the scope of today's financing problems, requests for IMF programs by many more countries must be anticipated over the next year, and it is probable that unless action is taken to increase IMF resources its ability to commit funds to future adjustment programs will be exhausted by late 1983 or early 1984. I will return to our specific proposals in this area shortly.

The IMF cannot be our only buffer in financial emergencies. It takes time for borrowers to design and negotiate lending programs with the IMF and to develop financing arrangements with other creditors. As we have seen in recent cases, the problems of troubled borrowers can sometimes crystallize too quickly for that process to reach its conclusion -- in fact, the real liquidity crunch came in the Mexican and Brazilian cases before such negotiations even started.

Thus, the third element in our strategy is the willingness of governments and central banks in lending countries to act quickly to respond to debt emergencies when they occur. Recent experience has demonstrated the need to consider providing immediate and substantial short-term financing -- on a selective basis, where system-wide dangers are present -- to tide countries through their negotiations with the IMF and discussions with other creditors.

We are undertaking this where necessary, on a case-by-case basis, through ad hoc arrangements among finance ministries and central banks, often in cooperation with the Bank for International Settlements. But it must be emphasized that these lending packages are short-term in nature, designed to last for only a year at most and normally much less, and cannot substitute for IMF resources which are designed to help countries through a multi-year adjustment process.

In fact, IMF resources themselves have only a transitional and supporting role. The overall amount of Fund resources, while substantial, is limited and not in any event adequate to finance all the needs of its members. While we feel that a sizeable increase in IMF resources is essential, this increase is not a substitute for lending by commercial banks. Private banks have been the largest single source of international financing in the past to both industrial and developing countries, and this will have to be the case in the future as well -- including during the crucial period of adjustment.

Thus, the fourth essential element in resolving debt problems is continued commercial bank lending to countries that are pursuing sound adjustment programs. In the last months of 1982 some banks, both in United States and abroad, sought to limit or reduce outstanding loans to troubled borrowers. But an orderly resolution of the present situation requires not only a willingness by banks to "roll over" or restructure existing debts, but also to increase their net lending to developing countries, including the most troubled borrowers, to support effective, non-disruptive adjustment. The increase in net new commercial bank lending needed for just three countries -- Brazil, Argentina, and Mexico -- will approach $11 billion in 1983. Without this continued lending in support of orderly and constructive economic adjustment, the programs that have been formulated with the IMF cannot succeed -- and the lenders have a strong self-interest in helping to assure success. It should be noted, however, that new bank lending will be at a slower rate than that which has characterized the last few years -- more in line with the increase in 1982 than what we saw in 1980 or 1981.

The final part of our strategy is to restore sustainable economic growth and to preserve and strengthen the free trading system. The world economy is poised for a sustained recovery: inflation rates in most major countries have receded; nominal interest rates have fallen sharply; inventory rundowns are largely complete.

Solid, observable U.S. recovery is one critical ingredient missing for world economic expansion. We believe the U.S. recovery is now getting underway, as evidenced by the recent drop in unemployment and upturns in orders and production. Establishing credible growth in other industrial economies is also important and we believe the base for recovery is being laid abroad as well.

However, both we and others must exercise caution at this turning point. Governments must not give in to political pressures to stimulate their economies too quickly through excessive monetary or fiscal expansion. A major shift at this stage could place renewed upward pressure on inflation and interest rates.

In addition, rising protectionist pressures, both in the United States and elsewhere, pose a real threat to global recovery and to the resolution of the debt problem. When one country takes protectionist measures hoping to capture more than its fair share of world trade, other countries will retaliate. The result is that world trade shrinks, and rather than any one country gaining additional jobs, everybody loses. More importantly for current debt problems, we must remember that export expansion by countries facing problems is crucial to their balance of payments adjustment efforts. Protectionism cuts off the major channel of such expansion. That adjustment is essential to restoring problem country debtors to sustainable balance of payments positions and avoiding further liquidity crises -- and as we have seen, it is therefore essential to the economic and financial health of the United States.

The only solution is a stronger effort to resist protectionism. As the world's largest trading nation, the United States carries a major responsibility to lead the world away from a possible trade war. The clearest and strongest signal for other countries would be for the United States to renounce protectionist pressures at home and to preserve its essentially free trade policies. That signal would be followed, and would reinforce, continued U.S. efforts to encourage others to open their markets, and would in turn be reinforced by IMF program requirements for less restrictive trade policies by borrowers.

The Role and Resources of the IMF

I have stressed the role of the International Monetary Fund in dealing with the current financial situation, and now I would like to expand on that point. The IMF is the central official international monetary institution, established to promote a cooperative and stable monetary framework for the world economy. As such, it performs many functions beyond the one we are most concerned with today -- that of providing temporary balance of payments financing in support of adjustment. These include monitoring the appropriateness of its members' foreign exchange arrangements and policies, examining their economic policies, reviewing the adequacy of international liquidity, and providing mechanisms through which its member governments cooperate to improve the functioning of the international monetary system.

In that context, it becomes clearer that IMF financing is provided only as part of its ongoing systemic responsibilities. Its loans to members are made on a temporary basis in order to safeguard the functioning of the world financial system -- in order to provide borrowers with an extra margin of time and money which they can use to bring their external positions back into reasonable balance in an orderly manner, without being forced into abrupt and more restrictive measures to limit imports. The conditionality attached to IMF lending is designed to assure that orderly adjustment takes place, that the borrower is restored to a position which will enable it to repay the IMF over the medium term. In addition, a borrower's agreement with the IMF on an economic program is usually viewed by financial market participants as an international "seal of approval" of the borrower's policies, and serves as a catalyst for additional private and official financing.

The money which the IMF has available to meet its members' temporary balance of payments financing needs comes from two sources: quota subscriptions and IMF borrowing from its members. The first source, quotas, represents the Fund's main resource base and presently totals some SDR 61 billion, or about $67 billion at current exchange rates. The IMF periodically reviews the adequacy of quotas in relation to the growth of international transactions, the size of likely payments imbalances and financing needs, and world economic prospects generally.

At the outset of the current quota discussions in 1981, many IMF member countries favored a doubling or tripling of quotas, arguing both that large payments imbalances were likely to continue and that the IMF should play a larger intermediary role in financing them. While agreeing that quotas should be adequate to meet prospective needs for temporary financing, the United States felt that effective stabilization and adjustment measures should lead to a moderation of payments imbalances, and that a massive quota increase was not warranted. Nor did we feel that an extremely large quota increase would be the most efficient way to equip the IMF to deal with unpredictable and potentially major financing problems that could threaten the stability of the system as a whole, and for which the IMF's regular resources were inadequate.

Accordingly, the United States proposed a dual approach to strengthening IMF resources:

- First, a quota increase which, while smaller than many others had wanted, could be expected to position the IMF to meet members' needs for temporary financing in normal circumstances.

- Second, establishment of a contingency borrowing arrangement that would be available to the IMF on a stand-by basis for use in situations threatening the stability of the system as a whole.

This approach has been adopted by the IMF membership, in agreements reached by the major countries in the Group of Ten in mid-January, and by all members at the IMF's Interim Committee meeting early last month.

The agreed increase in IMF quotas is 47 percent, an increase from SDR 61 billion to SDR 90 billion (in current dollar terms, an increase from $67 billion to $99 billion). The proposed increase in the U.S. quota is SDR 5.3 billion ($5.8 billion at current exchange rates) representing 18 percent of the total increase.

The Group of Ten, working with the IMF's Executive Board, has agreed to an expansion of the IMF's General Arrangements to Borrow from the equivalent of about SDR 6.5 billion at present to a new total of SDR 17 billion, and to changes in the GAB to permit its use, under certain circumstances, to finance drawings on the IMF by any member country. Under this agreement, the U.S. commitment to the GAB would rise from $2 billion to SDR 4.25 billion, equivalent to an increase of roughly $2.7 billion at current exchange rates.

We believe this expansion and revision of the GAB offers several important attractions and, as a supplement to the IMF's quotas, greatly strengthens the IMF's role as a backstop to the system:

-- First, since GAB credit lines are primarily with countries that have relatively strong reserve and balance of payments positions, they can be expected to provide more effectively usable resources than a quota increase of comparable size. Consequently, expansion of the GAB is a more effective and efficient means of strengthening the IMF's ability to deal with extraordinary financial difficulties than a comparable increase in quotas.

-- Second, since the GAB will not be drawn upon in normal circumstances, this source of financing will be conserved for emergency situations. By demonstrating that the IMF is positioned to deal with severe systematic threats, an expanded GAB can provide the confidence to private markets that is needed to ensure that capital continues to flow, thus reducing the risk that the problems of one country will affect others.

-- And third, creditors under this arrangement will have to concur in decisions on its activation, ensuring that it will be used only in cases of systemic need and in support of effective adjustment efforts by borrowing countries.

Annex A to my statement contains the texts of the relevant IMF report and decisions on the quota increase and GAB revisions. In sum, the proposed increase in U.S. commitments to the IMF totals SDR 7.7 billion -- SDR 5.3 billion for the increase in the U.S. quota and SDR 2.4 billion for the increase in the U.S. commitment under the GAB. At current exchange rates, the dollar equivalents are $8.5 billion in total, $5.8 billion for the quota increase and $2.7 billion for the GAB increase.

We believe these steps to strengthen the IMF, if enacted, will safeguard the IMF's ability to respond effectively to current financial problems. Given the financing needs we foresee, we feel it is important that the increases be implemented by the end of this year. Without such a timely and adequate increase in IMF resources, the ability of the monetary system to weather debt and liquidity problems will be impaired, at substantial direct and indirect cost to the United States.

The U.S. share in the increase in IMF resources is 18 percent, which obviously means other countries are putting up the remaining 82 percent, the great bulk of the increase. By putting up 18 percent of the increase, we will maintain our voting share at just over 19 percent. The principle of weighted voting on which the IMF operates has been key to its effectiveness over the years and to ensuring that we have a voice and vote comparable to the share of resources we provide. Major policy decisions -- such as those just taken on the quota increase -- require an 85 percent majority vote, giving us a veto over all such decisions. Some of our allies would claim that we aren't pulling our own weight -- that our stake in world trade and finance is bigger than the share of resources we are proposing to put into the IMF would indicate.

While fundamentally the IMF is designed to further our economic interests, in so doing it also benefits U.S. political and security interests. The IMF is essentially a non-political institution, with membership open to any country judged willing and able to meet the obligations of membership. But it serves our interests well by containing economic problems which could otherwise spread through the international community; as a stabilizing element in countries facing the social and economic dislocations which can accompany adjustment; and supporting open, market-oriented economic systems consistent with Western political values. Judged on this criterion, U.S. appropriations for the IMF can be an excellent investment if they can help to avoid political upheaval in countries of critical interest to the United States.

<u>Concerns about the Increase in IMF Resources</u>

The general outline of our proposals has been known to members of Congress for some time. Many have expressed reservations or questions about this proposal, and I would like to discuss some of the main concerns now.

° <u>Is the IMF "Foreign Aid"?</u>

Many perceive money appropriated for IMF use to be just another form of foreign aid, and question why we should be providing U.S. funds to foreign governments. Let me assure you that the IMF is <u>not</u> a development institution. It does not finance dams, agricultural cooperatives, or infrastructure projects. The IMF <u>is</u> a <u>monetary</u> institution. Only one of its functions is providing balance of payments financing to its members in order to promote orderly functioning of the monetary system, and only then on a temporary basis, on medium-term maturities, after obtaining agreement to the fulfillment of policy conditions. We have been working very hard with the IMF to ensure that both the effectiveness of IMF policy conditions, and the temporary nature of its financing, are safeguarded. In this way, the Fund's financing facilities will continue to have a revolving nature and to promote adjustment.

IMF conditionality has been controversial over the years, with strong opinions on both sides. Some observers have worried that conditionality is so weak and ineffective that conditional lending is virtually a giveaway. Others believe that conditionality is too tight -- that it imposes unnecessary hardship on borrowers, and stifles economic growth and development.

Such generalizations reflect a misunderstanding of IMF conditionality. When providing temporary resources to a country faced with external financing problems, the IMF seeks to assure itself that the country is pursuing policies that will enable it to live within its means -- that is, within its ability to obtain foreign financial resources. It is this that determines the degree of adjustment that is necessary. It is often the case that appropriate economic policies will strengthen a country's borrowing capacity, and result in both higher import growth and higher export growth. I would cite the example of Mexico as an immediate case in point.

Mexico is our third largest trading partner, after Canada and Japan. And, as recently as 1981, it was a partner with whom we had an export boom and a substantial trade surplus, exporting goods to meet the demands of its rapidly growing population and developing economy. This situation changed dramatically in 1982, as Mexico began experiencing severe debt and liquidity problems. By late 1982, Mexico no longer had access to financing sufficient to maintain either its imports or its domestic economic activity. As a result, U.S. exports to Mexico dropped by a staggering 60 percent between the fourth quarter of 1981 and the fourth quarter of 1982. Were our exports to Mexico to stay at their depressed end-1982 levels, this would represent a $10 billion drop in exports to our third largest market in the world. Because the financing crunch got worse as the year wore on, totals for the full year 1982 don't tell the story quite so dramatically -- but even they are bad enough. Our $4 billion trade surplus with Mexico in 1981 was transformed into a trade deficit of nearly $4 billion in 1982, due mainly to an annual-average drop in U.S. exports of one-third. (Chart I.) This $8 billion deterioration was our worst swing in trade performance with any country in the world, and it was due almost entirely to the financing problem.

We believe that now this situation will start to turn around, and we can begin to resume more normal exports to Mexico. If this happens, it will be due in large part to the fact that, late in December, an IMF program for Mexico went into effect; and that program is providing the basis not only for IMF financing, but for other official financing and for a resumption of commercial bank lending as well. Mexico must make difficult policy adjustments if it is to restore creditworthiness. The Mexican authorities realize this and are embarked on a courageous program. But the existence of IMF financing and the other financing associated with it will permit Mexico to resume something more like a normal level of economic activity and imports while the adjustment takes place in an orderly manner. Without the IMF program, all we could look forward to would be ever-deepening depression in Mexico and still further declines in our exports to that country.

There is another aspect of the distinction between IMF financing and foreign aid which we should be very clear on, since it goes to the heart of U.S. relations with the Fund. All IMF members provide financing to the IMF under their quota subscriptions, and all -- industrial and developing alike -- have the right to draw on the IMF.

Quota subscriptions form a kind of revolving fund, to which all members contribute and from which all are potential borrowers.

As an illustration, in practice our quota subscription has been drawn upon many times -- and repaid -- over the years for lending to other IMF members. We in turn have drawn on the IMF on 24 occasions -- most recently in November 1978 -- and our total cumulative drawings, amounting to the equivalent of $6.5 billion, are the second largest of any member (the United Kingdom has been the largest user of IMF funds). (U.S. drawings on the IMF are described at Annex B.)

° Do IMF Programs Hurt U.S. Exports?

There is a widespread perception that IMF programs are designed to cut imports by countries which use IMF financing, and thus hurt U.S. exports to those countries. Some would argue, in fact, that far from helping to maintain world trade and U.S. exports, our participation in the increase in IMF resources would contribute to further reductions in our exports.

This is simply a misreading of the IMF. The whole point of an IMF program is to get a borrower's external balance back within sustainable limits -- but to judge the effects of those programs on our exports you always have to start by asking what would have happened without an IMF program. When a country draws on IMF financing, it usually does so in recognition of the fact that its external deficit is not going to be sustainable if it stays on its present course. If the borrower didn't go to the IMF, it would likely be cut off from further external financing from other sources and would have to cut back drastically on imports, as we saw in the case of Mexico.

Furthermore, IMF programs are not just directed at slowing the growth of imports. Reducing import growth is often one of the short-run necessities, but even then IMF financing can permit a higher level of imports than would otherwise be the case. And equally important are steps to increase a country's export capacity, thereby giving it the ability to pay for higher imports in the long run.

Exchange rate devaluations are often an important part of IMF programs -- devaluations intended to ensure that the right price signals are sent to domestic producers, importers and exporters, and that the competitiveness of domestic industries is restored. These devaluations have often been accompanied by the removal of restrictions on trade and capital flows. And, to lay one total misunderstanding to rest, an IMF program never calls for the tightening of import restrictions -- in fact, new or intensified restrictions are expressly prohibited. The IMF does not promote restrictions -- its purposes and policies go precisely in the opposite direction.

° Why Not Spend the Money at Home?

Another major concern with the proposals to increase IMF resources is that, in this period of budgetary stringency, many believe we would be better advised to spend the money at home. There is also some feeling that if we were to get the U.S. economy moving forward again, the international financial problem would take care of itself. I think I've already been through part of the response to these concerns when I described the large and growing impact which foreign trade now has on American growth and employment. We will do what is necessary domestically to strengthen our economy. But we will leave a major threat to domestic recovery unaddressed if we do not act to resolve the international financial situation. The direct impact alone of international developments on our economy is so large that, were the international situation not to improve, there would at a minimum be a tremendous drag on our economic recovery.

It is true that an improving U.S. economy is going to help other nations, both through our lower interest rates and through an expanding U.S. market for their exports -- providing of course that we don't cut them off from that market. But they also have an immediate, short-run financing crunch to get through, and if we don't handle that right there are substantial downside risks for the United States.

° Budgetary Treatment

This might also be the right context in which to discuss how U.S. participation in the increase in IMF resources would affect the Federal budget and the Treasury's borrowing requirements. Under budget and accounting procedures adopted in connection with the last IMF quota increase, in consultation with the Congress, both the increase in the U.S. quota and the increase in U.S. commitments under the GAB will require Congressional authorization and appropriation. However, because the United States receives a liquid, interest-earning reserve claim on the IMF in connection with our actual transfers of cash to the IMF, such transfers do not result in net budget outlays or an increase in the Federal budget deficit.

Actual cash transactions with the IMF, under our quota subscription or U.S. credit lines, do affect Treasury borrowing requirements as they occur. The amount of such transactions in any given year depends on a variety of factors, including the rate at which IMF resources are used; the degree to which the dollar in particular is involved in both current IMF drawings and repayments of past drawings; and whether the United States itself draws on the IMF.

An analysis appended to this statement at Annex C presents data on the impact of U.S. transactions between U.S. fiscal year 1970 and the first quarter of fiscal 1983 on Treasury borrowing requirements. Although there have been both increases and decreases in Treasury borrowing requirements from year to year, on average there have been increases amounting to about $1/2 billion annually over the entire period, for a cumulative total of about $7 billion. The rate has picked up in the last two years of heavy IMF activity, as would be expected; but the total is still relatively small -- the $1/2 billion annual impact is only a small part of the $61 billion annual average increase in Treasury borrowing over the same period, and the roughly $7 billion cumulative impact compares with an outstanding Federal debt of $1.1 trillion at the end of fiscal 1982. These figures also serve to demonstrate the revolving nature of the IMF.

° Is the IMF a Bank "Bail-Out"?

I also know there is a widespread concern that an increase in IMF resources will amount to a bank bail-out at the expense of the American taxpayer. Many would contend that the whole debt and liquidity problem is the fault of the banks -- that they've dug themselves and the rest of us into this hole though greed and incompetence, and now we intend to have the IMF take the consequences off their hands. This line of argument is dangerously misleading, and I would like to set the record straight.

First, the steps that are being taken to deal with the financial problem, including the increase in IMF resources, require continued involvement by the banks. Far from allowing them to cut and run, orderly adjustment requires increased bank lending to troubled LDCs that are prepared to adopt serious economic programs. That is exactly what is happening.

And it is not a departure from past experience. I have had Treasury staff review IMF program experience in the 20 countries which received the largest net IMF disbursements in the last few years, to see whether banks had been "bailed out" in the past. Looking at the period from 1977 to mid-1982, they found that for the countries which rely most heavily on private bank financing, IMF programs have been followed up by new bank lending much greater than the amount disbursed by the Fund itself. This also holds true for the 20 countries as a group: net IMF disbursements to this group during the period were $11.5 billion, while net bank lending totalled $49.7 billion, resulting in a ratio of 4.3 to 1 during this period.

Another point I would like to make is that the whole debt and liquidity problem cannot fairly be said to be the fault of the commercial banks. In fact, the banking system as a whole performed admirably over the last decade, in a period when there were widespread fears that the international monetary system would fall apart for lack of financing in the aftermath of the oil shocks. The banks managed almost the entire job of "recycling" the OPEC surplus and getting oil importers through that difficult period. Some of the innovations and decisions that banks made in the process, which seemed rational and necessary at the time to them and to others, may seem doubtful in retrospect, given the way the world economic environment changed. But I think we can agree that governments have had a great deal more to do with shaping that environment than banks.

All of this is not to say that there aren't lessons to be learned in the banking area. We should be asking ourselves: What is there that banks could be doing to improve their screening of foreign loans? What is there that bank regulators could do to improve on their analysis of country risk, examination of bank exposure, and consultations with senior management?

Our basic starting point in addressing these questions is a belief that the U.S. government should not get into the business of dictating the lending practices of private banks. Doing so would inject a political element into what should be business decisions, and would potentially expose the government to liability for covering loans that were not repaid on time. Moreover, in general it is bank managements, which have direct experience and a responsibility to their shareholders and depositors to motivate them, that are in the best position to make lending decisions.

In 1979, the bank regulatory agencies (the Federal Reserve, Comptroller of the Currency and the FDIC) instituted a new system for evaluating country risk, which has four elements. The first is a statistical reporting system designed to identify country exposures at each bank, and to enable regulators to monitor those exposures. Second is an evaluation of each bank's internal system for managing country risk, aimed at encouraging more systematic review of prospective loans. Third, where there is a judgment by regulators that a country has interrupted its debt service payments, or is about to do so, all loans to that country may be "classified" as substandard, doubtful, or a total loss, and such "classification" may trigger an obligation by the bank to set aside precautionary loan loss reserves. Fourth, bank examiners review and comment upon each bank's large foreign lending exposures, drawing upon the findings of an interagency committee of country analysts.

Several possible changes in the regulatory environment have been suggested. Both in the banking regulatory agencies, and at the Treasury, we will be reviewing the possibilities to see what changes might be desirable. We need to be careful in determining how to deal with such a sensitive and central part of our economy. The issues are complex. Some possible steps could be harmful to our economic interests, and any decisions in this area will have important implications both for resolving the present situation and for the evolution of the banking system in the future.

The Multilateral Development Banks

The objectives of the multilateral development banks (MDBs) are markedly different from those of the IMF. They lend primarily to finance portions of specific investment projects, both on near-market terms from their "hard" windows, and on concessional terms from their "soft" windows. MDB financing is longer term -- 20 years or more -- and it is available only to developing countries. The institutions included in this category include the World Bank Group (the International Bank for Reconstruction and Development, International Development Association and International Finance Corporation), and the regional development banks (the Inter-American Development Bank, Asian Development Bank, and African Development Bank and Fund). These institutions have all been established in the period since World War II and they are now an important part of the international economic and financial system. The United States played a leading role in the founding of all but the African Development Bank and plays a leading role in the continuing operations of all the MDBs.

The banks are owned by share-holding member countries including the United States, other industrial countries, OPEC countries and non-OPEC LDCs. The cumulative U.S. share of the MDBs ranges from 58 percent of the Inter-American Development Bank's Fund for Special Operations to 6 percent of African Development Bank capital. The overall United States share of MDB resources has been declining, and currently stands at one-quarter of MDB resources.

The purpose of the MDBs is to promote sustainable economic growth and social development in their less developed member countries. To this end, they make loans on both near-market and concessional terms to help finance projects and programs in all major economic sectors. Many of these projects supply basic needs, while others are aimed primarily at providing the infrastructure necessary for stronger long-term economic growth and employment. The banks also provide borrowing countries with technical assistance in planning and implementing projects, and training and help to improve their public and private institutions. They advise recipient governments on appropriate economic policy choices, and coordinate and encourage the flow of public and private capital to LDCs. By effectively promoting developing country growth, the MDBs also contribute to the growth and stability of the world economy.

For U.S. participation in the MDBs during FY 1984, we are requesting $1.6 billion in budget authority. Of this amount, $193 million is for subscriptions to paid-in capital and the remaining $1,406 million is for our contributions to the concessional windows of the MDBs for lending to the poorest, least creditworthy countries. The actual budgetary outlays resulting from these subscriptions and contributions would be spread over a period of many years since they are drawn primarily as required to meet loan disbursement needs.

The outlay pattern for the $1.6 billion requested for FY 1984 is typical. It is estimated that only 4.3 percent of the request would result in outlays in FY 1984, 7.3 percent in FY 1985 and 10.8 percent in FY 1986. Such an outlay pattern means that in any given year practically all MDB budget outlays result from subscriptions and contributions made in prior years.

In addition to the budget authority we are also requesting $2.9 billion in program limitations for subscriptions to the callable capital of the MDBs. The "callable capital" concept is one of the attractive features of the multilateral development banks and results in considerable budgetary savings for the U.S. government. With callable capital as backing, the MDBs are able to borrow most of the non-concessional funds they require in international capital markets. The cost to the U.S. Government of subscriptions to callable capital is solely contingent in nature, since callable capital can only be used to meet obligations of the MDBs for funds they have borrowed or guaranteed, in the unlikely event that their other resources were insufficient to meet those liabilities.

The individual items of the MDB request for FY 1984 are detailed in the table attached as Annex D. The request includes paid-in capital subscriptions and contributions to the concessional windows totaling $1,281 million of budget authority for which authorization legislation has been received and $337 million of budget authority that has yet to be authorized. The FY 1984 request also includes $1,407 million of previously authorized program limitations for callable capital subscriptions and $1,455 million of program limitations which have yet to be authorized.

The replenishments and capital increases for which we will be seeking authorization reflect the implementation of the recommendations made as a result of our assessment of U.S. participation in the MDBs. The MDB assessment concluded that the MDBs are a cost-effective way to contribute to LDC growth and stability; and that through them the U.S. can and should encourage adherence to free and open markets, emphasis on the private sector, minimal government involvement, and assistance to countries who demonstrate the ability to make good use of available resources. In short, the banks are proven, effective instruments for promoting economic growth and development.

Since U.S. interests can be well served by these institutions, we have been focusing on ways to make their programs more effective. In specific terms, we have been working with the banks to ensure: (1) greater selectivity and policy conditionality within projects and sector programs to encourage sound economic policies conducive to sustainable growth; (2) more emphasis on catalyzing private sector flows and promoting LDC private sector development; (3) firm implementation of graduation from hard windows to market borrowing, and maturation from soft windows to hard, in order to distribute MDB resources to those countries with the greatest need; and (4) reduction in the rates of growth of MDB programs, particularly for soft-loan windows.

The Eximbank Budget

The Administration's export credit policy continues to be based on three precepts:

(1) We oppose export credit subsidies. Such subsidies transfer resources from domestic taxpayers to foreign importers, reduce the real gains from exporting, distort trade, and result in bloated government demands on credit markets.

(2) Export credit subsidies should be reduced and eventually eliminated through international agreement.

(3) In instances where such subsidies are applied, financing from the Export-Import Bank of the United States should be targeted to meet the competition where it is greatest.

Eximbank has an important role in supporting U.S. exporters against foreign predatory financing, helping to overcome imperfections in capital markets, and maintaining pressure on other governments to negotiate reductions in their own export credit subsidies.

We are requesting budget authority for the Export-Import Bank of the United States of $3.8 billion in direct credits and $10.0 billion in guarantees and insurance for FY 1984. In addition, we have pledged that we will request supplemental direct credit authority of up to $2.7 billion, if foreign subsidized financing again emerges as a serious problem.

These requests reflect both the Administration's long-run export credit policy and the emerging financial environment. Increased support for U.S. exports through guarantees and insurance is designed to encourage the continued availability of credit for U.S. exports at a time when LDC debt problems make commercial lenders more cautious. The level direct credit authority we are requesting reflects expected economic trends, as well as an effort to increase the use of long-term guarantees. Our pledge to seek supplemental authority, if needed, shows the U.S. commitment to offer competitive support in the face of heavily subsidized foreign financing, should this again become a problem.

The Administration's budget requests for Eximbank respond to fundamental changes in the export financing environment which have occurred during the past year. Some analyses of export finance are warped by the experience of the last five years, which have been characterized by heavily subsidized export credits. During this period, the primary objective of Eximbank has been to nuetralize the effects of predatory export credit financing by other countries. Eximbank's direct credit program remained competitive with foreign officially-supported export credits, as is shown by its relatively high "win" ratio. Few cases were lost because of financing.

Eximbank remained competitive, however, at a very high price, since its cost of money exceeded its lending rate from the fourth quarter of 1978 until the fourth quarter of 1982. As a result, Eximbank's net income dropped until the Bank realized its first losses during FY 1982. This negative net income is projected to continue for at least four more years.

The export credit picture has changed dramatically in the past year. Our two-year quest to eliminate export credit subsidies has largely been achieved due to the recent convergence of commercial interest rates and officially-supported interest rates. The U.S. Treasury has successfully negotiated improvements in the OECD

Arrangement on Export Credits, which have significantly raised the minimum interest rates offered by foreign export credit agencies. At the same time, commercial interest rates have declined as a result of our success in bringing down inflation. As a result, the Eximbank Board has recently been able to reduce the interest rates the Bank charges on its loans to the lowest levels permitted under the International Arrangement on Export Credits.

Fundamentally lower interest rates in all SDR currencies except the French franc coupled with much higher interest rate minima under the Arrangement than a year ago present an opportunity for Eximbank to make increasing use of guarantee and insurance authority in the provision of competitive financing offers. Moreover, current trends in U.S. market rates and the expected financial status of many developing country borrowers may well enhance the shift of demand from credits to guarantees, since commercial lenders may require this additional inducement to increase trade credit to some countries.

Thus, the critical issues for trade finance are shifting in this new environment. Export credit subsidies will fade and perhaps disappear as key elements in export credit competition. Instead, the availability of export finance will take center stage in a world in which commercial export credits may become more difficult to obtain.

Conclusion

The IMF plays a crucial role in the solution to current debt and liquidity problems, and in providing the environment for world recovery. It is absolutely essential that the proposed increase in IMF resources become effective by the end of this year, to enable the IMF to meet these responsibilities. Prompt U.S. approval is important not only because the financing is needed, but also because it would be a sign of confidence to other governments and to the public, and would help lay to rest concerns about the risks to global recovery posed by the international debt problem.

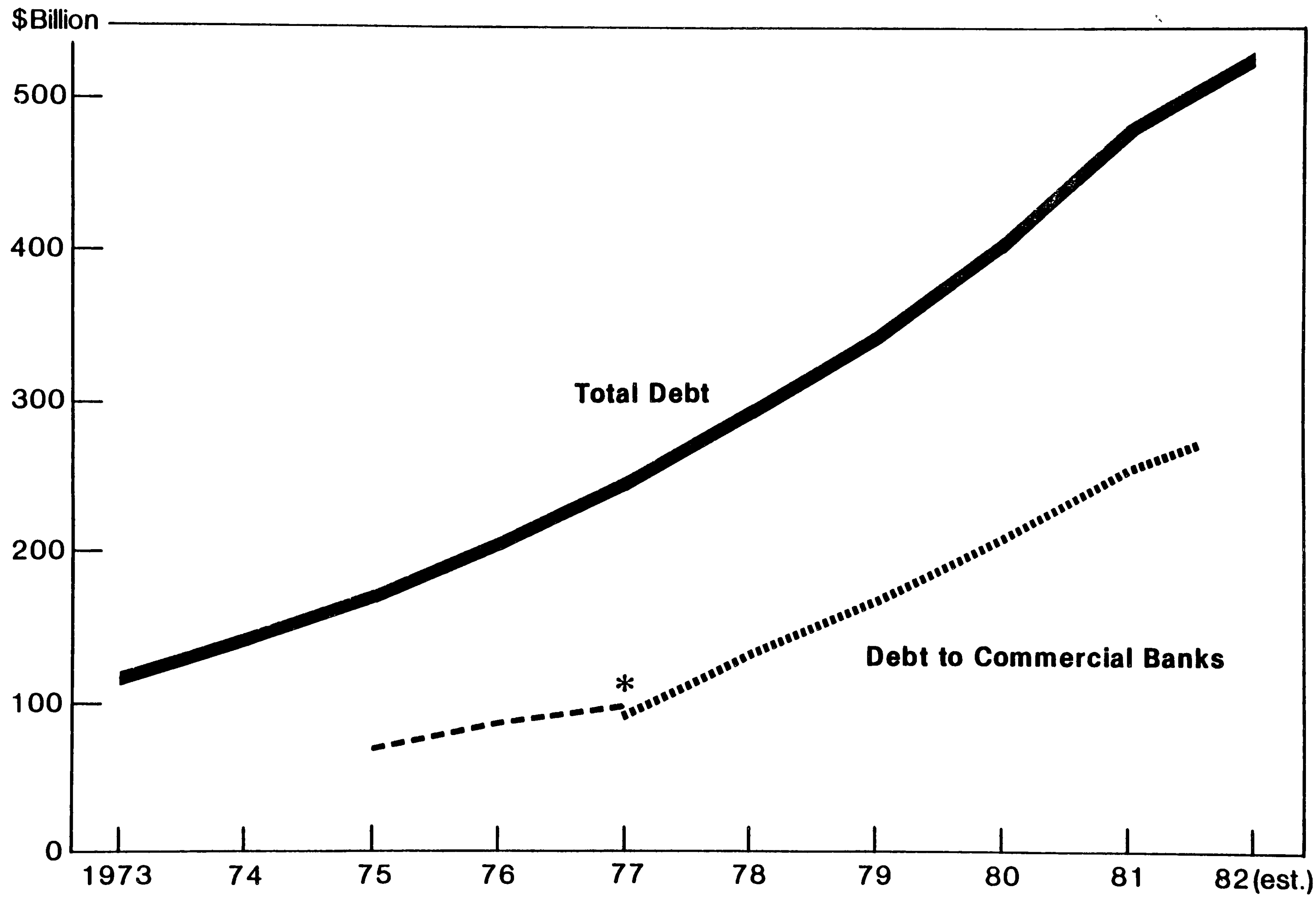
But most importantly, timely approval of these proposals is essential to our own economic interests -- to the prospects for American businesses and American jobs. As I have indicated, we are making a substantial effort to support U.S. exports through Eximbank financing next year; but keeping the debt problem from mushrooming into a financial crisis would do much more to safeguard prospects for the expansion of world trade and U.S. exports. I urge that you give the proposed legislation authorizing and appropriating our participation in the increase in IMF resources prompt and favorable consideration.

Both the IMF and the multilateral development banks also serve broader U.S. political and security interests. To the rest of the world they are a sign that the bulwark of democracy is also a responsible partner in international economic affairs. To the poorer nations of the world the multilateral development banks are also tangible evidence of the support by Western nations for sustainable economic development. And of direct benefit to the United States, they help to foster political stability and democratic values in the developing world.

I have tried to lay out a number of reasons for the United States to support the IMF, the MDBs, and the Eximbank. Most of these reasons relate significantly to our own interests. I urge your strong support for the proposed U.S. appropriations for these institutions.

Chart A

OUTSTANDING FOREIGN DEBT OF NON-OPEC LDCs

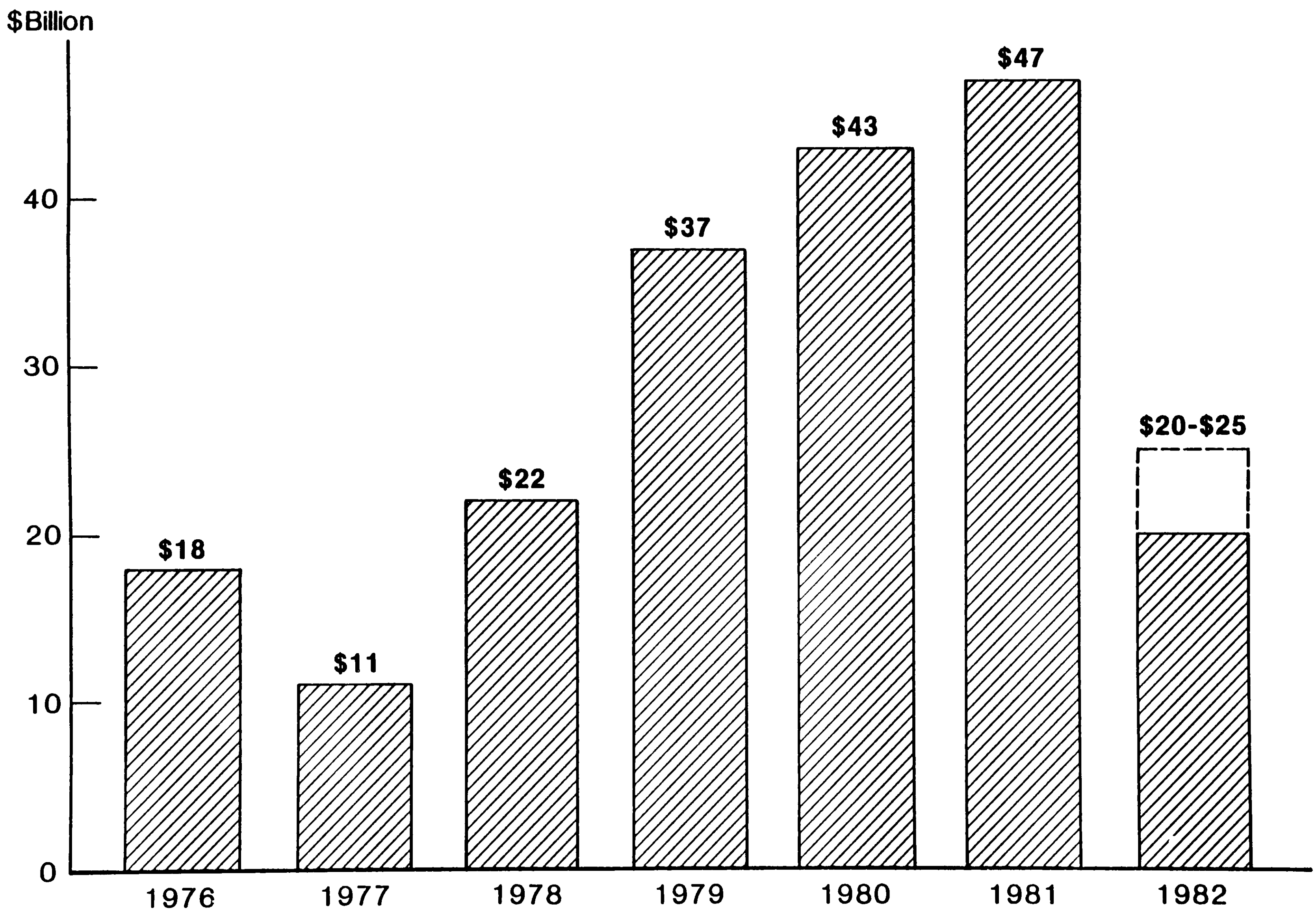


* Series break.

U.S. Treasury Dept.
2-11-83

Chart B

NET NEW LENDING BY COMMERCIAL BANKS TO NON-OPEC LDCs



U.S. Treasury Dept.
2-11-83

Chart C

GROWTH OF U.S. AND WORLD EXPORT VOLUME

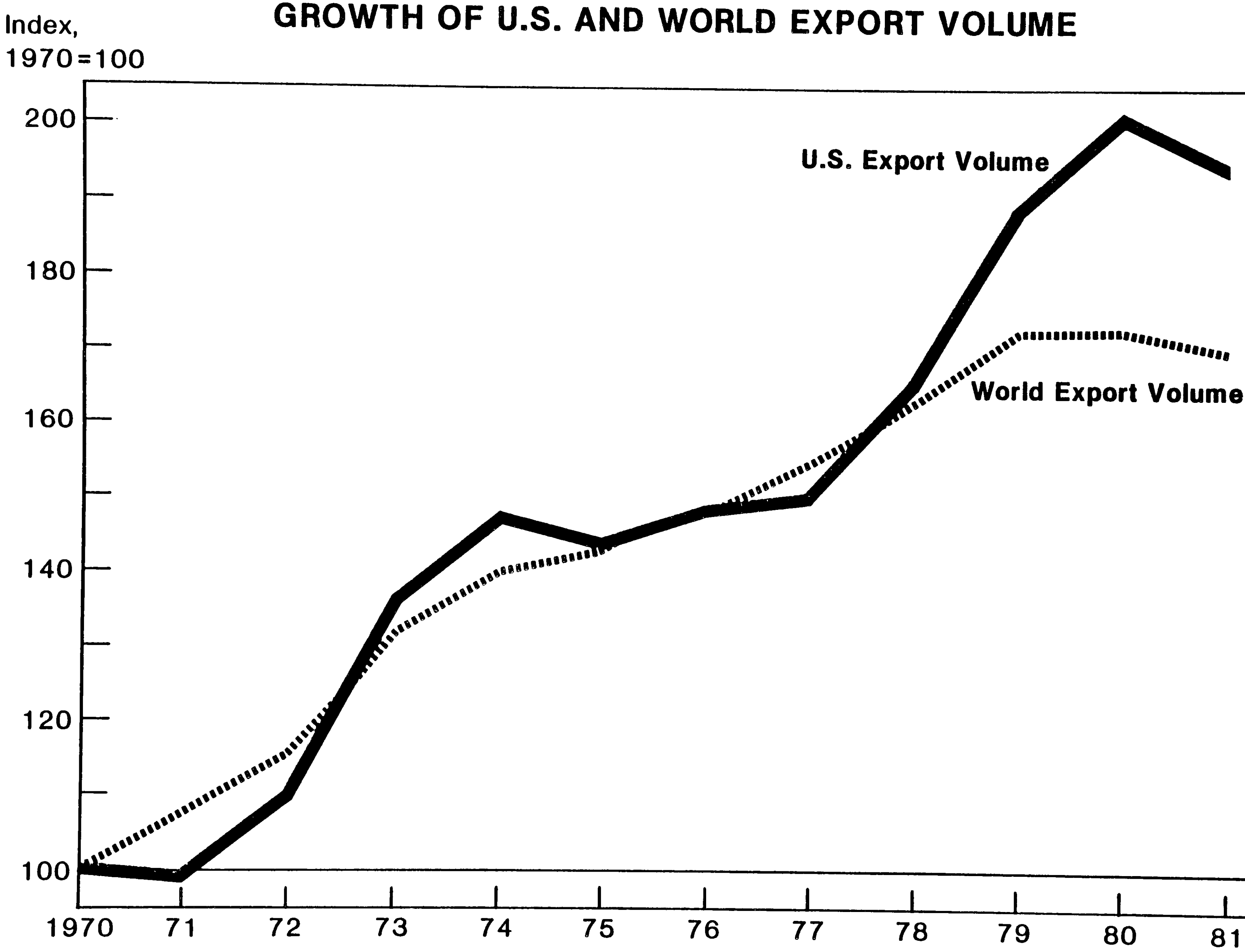
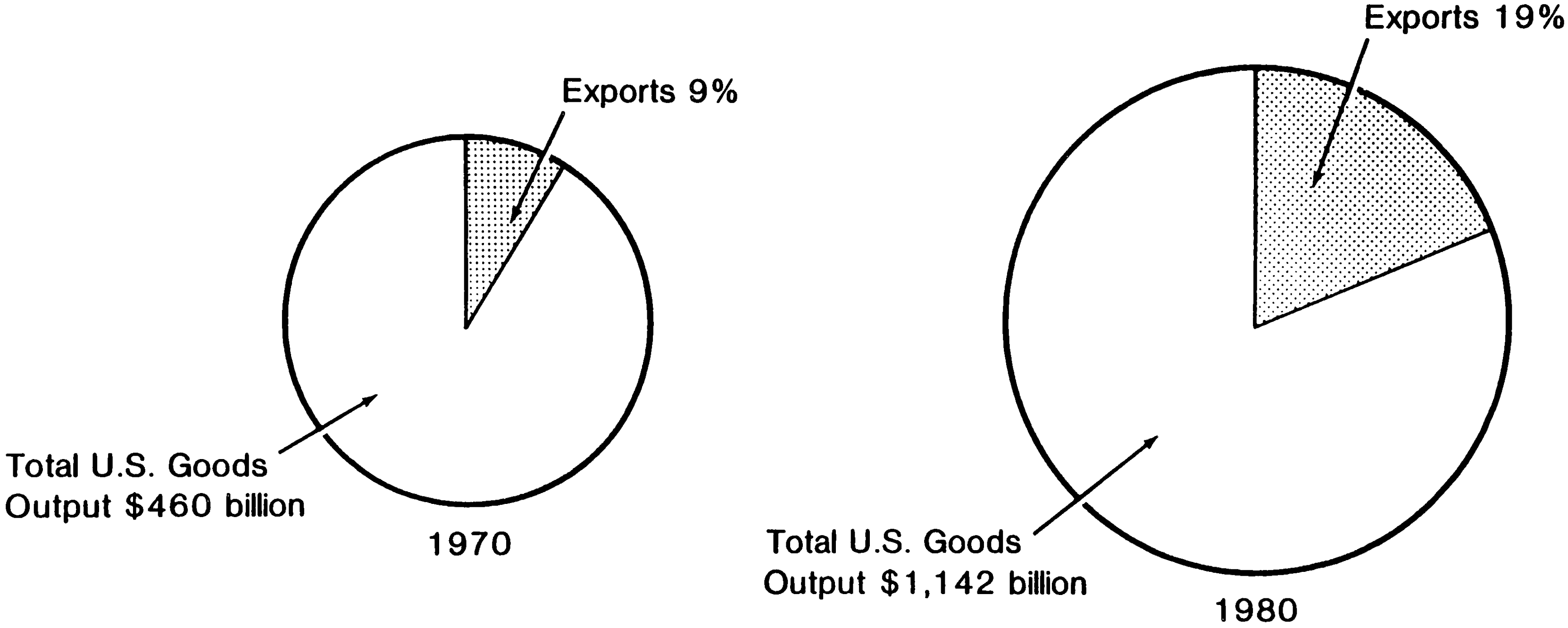


Chart D

SHARE OF U.S. EXPORTS IN TOTAL U.S. GOODS OUTPUT

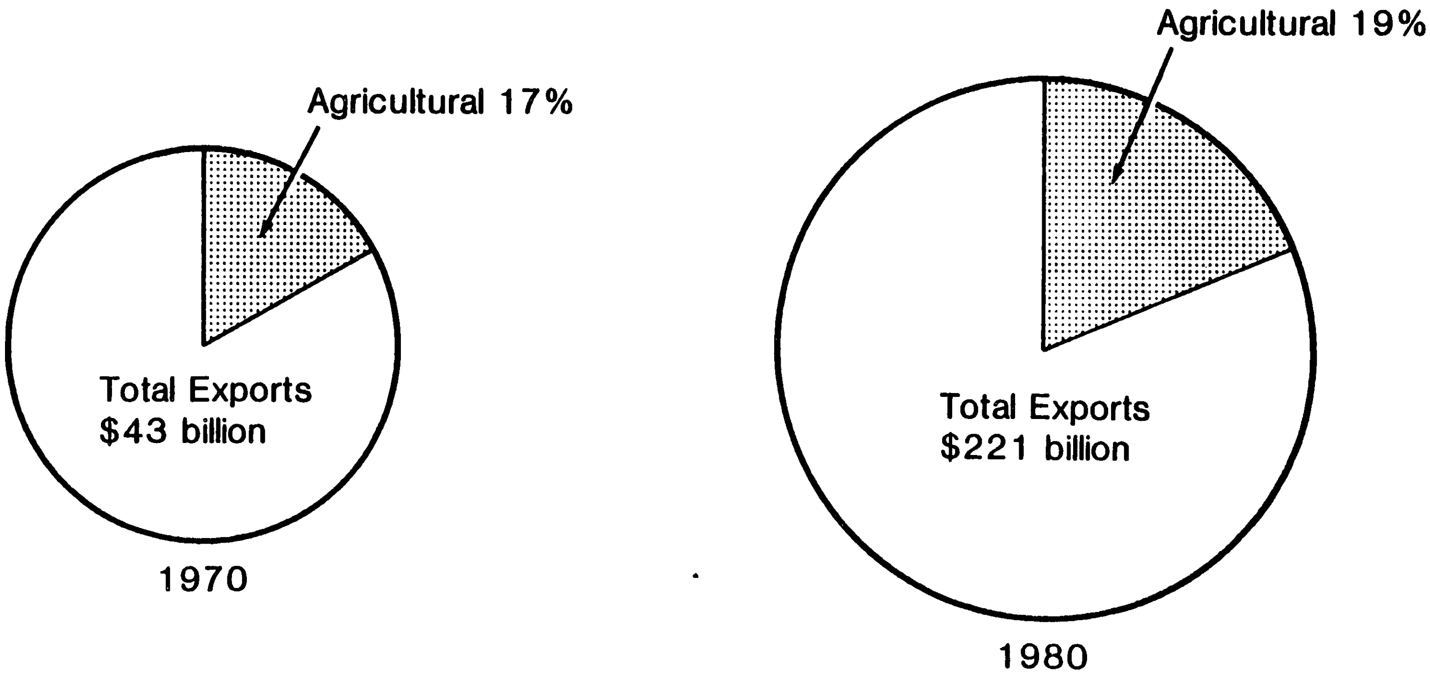


U.S. Treasury Dept.
2-11-83

Chart E

U.S. AGRICULTURAL EXPORTS

Share in Total U.S. Exports:



Net U.S. Agricultural Trade Balance:

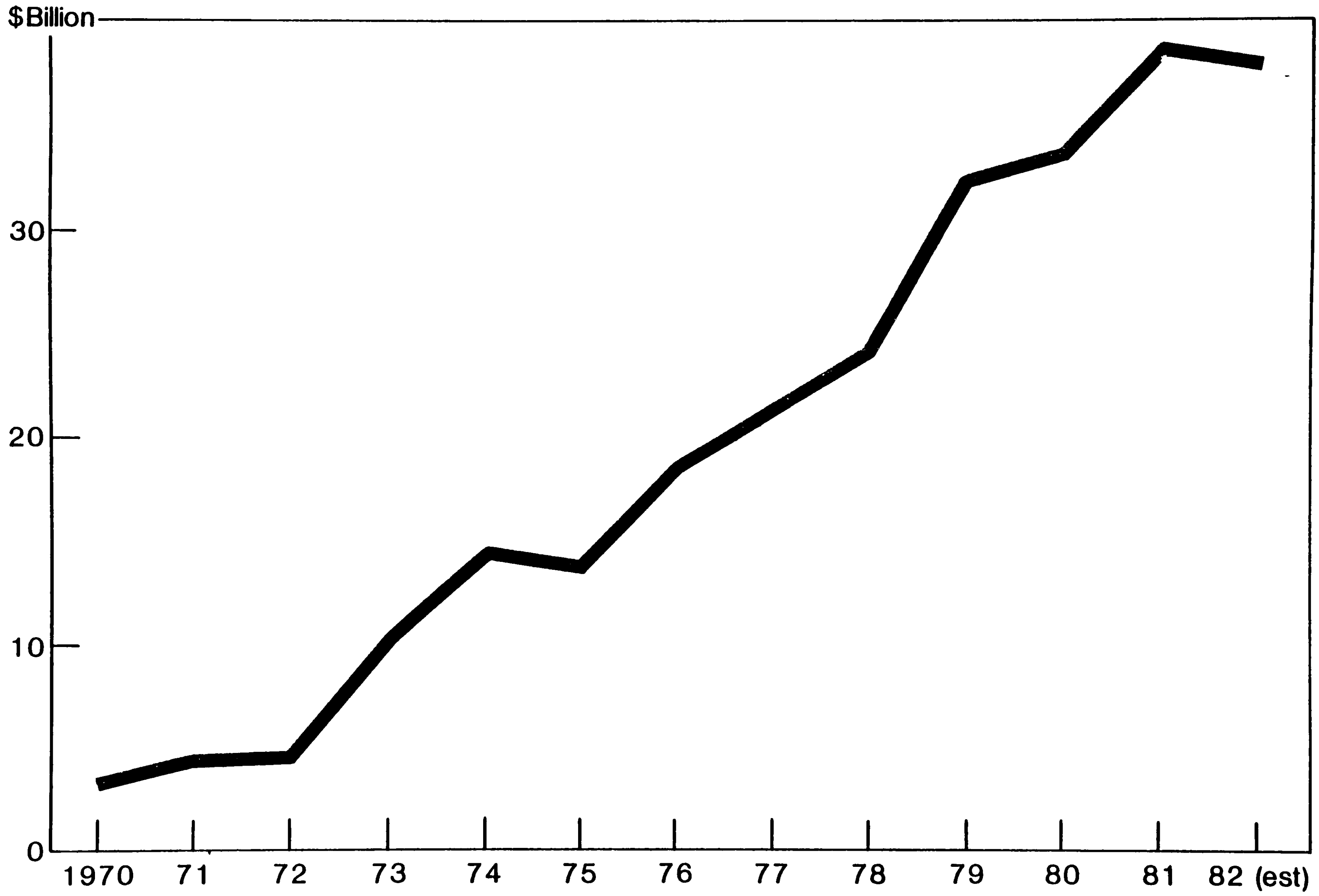
Surplus of $1.6 billion

Surplus of $24.3 billion

U.S. Treasury Dept.
2-11-83

Chart F

U.S. TRADE BALANCE IN SERVICES



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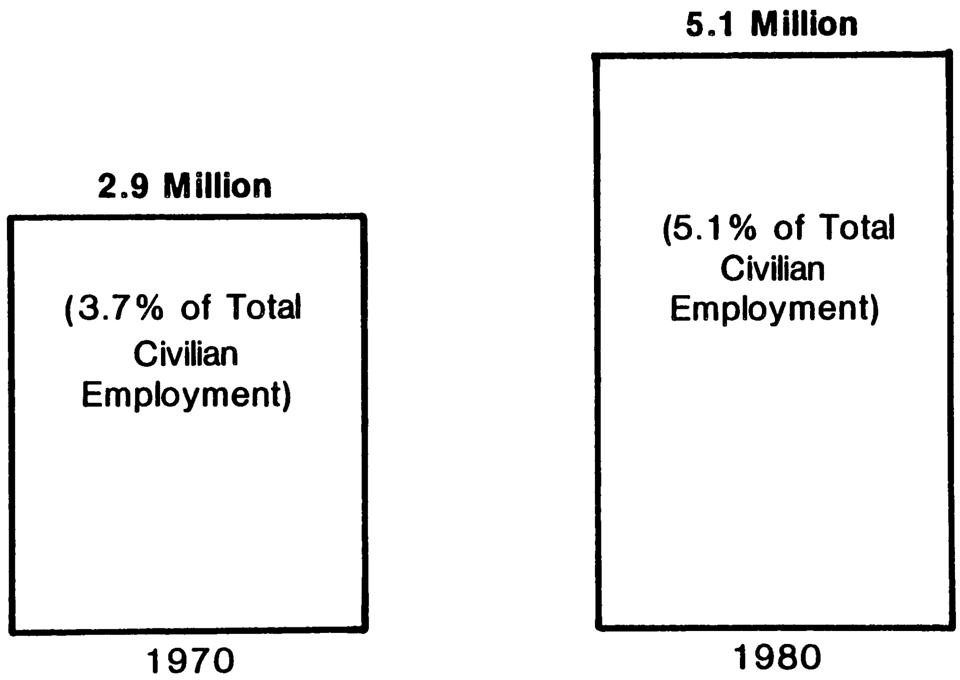
2-11-83

Chart G

U.S. EXPORT-RELATED JOBS



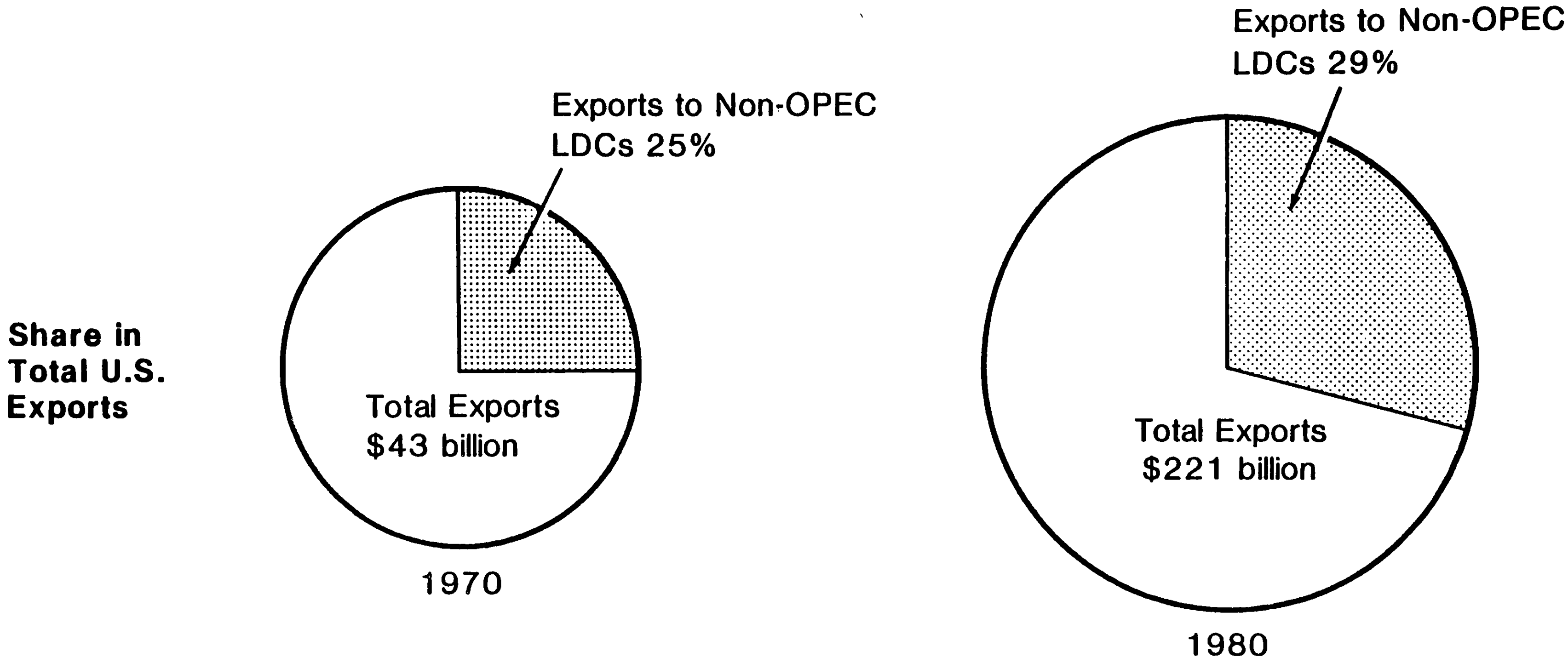
As of 1980, each $1 billion of U.S. exports was estimated to result in 24,000 jobs.

Source: Commerce Department (ITA) estimates.

U.S. Treasury Dept.
2-11-83

Chart H

U.S. EXPORTS TO NON-OPEC LESS DEVELOPED COUNTRIES



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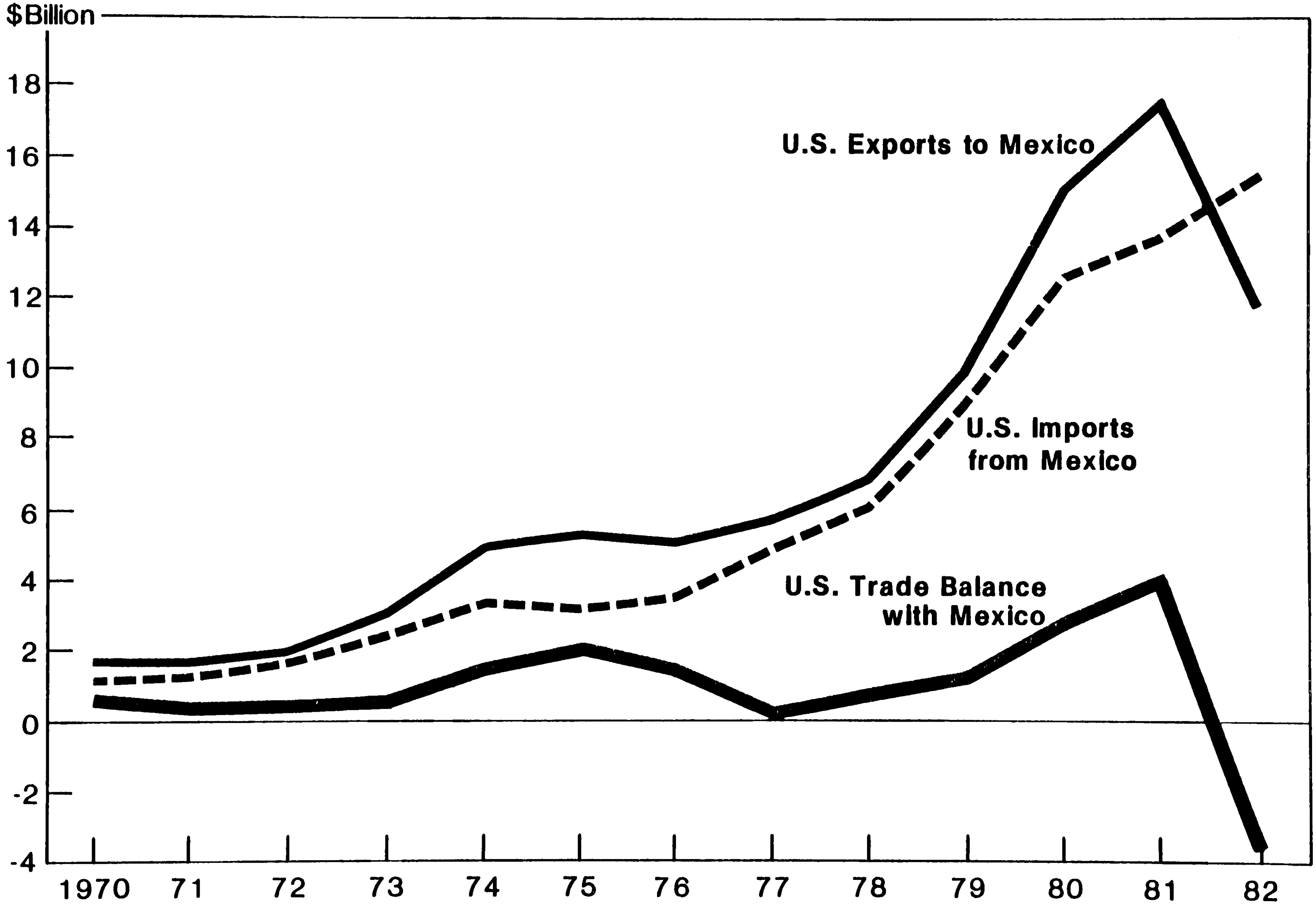
2-11-83

Chart I

U.S. TRADE WITH MEXICO



U.S. Treasury Dept.
2-11-83

INTERNATIONAL MONETARY FUND

PRESS RELEASE NO. 83/17

FOR IMMEDIATE RELEASE
March 1, 1983

The Executive Board of the International Monetary Fund has taken two actions which, when they become effective, will substantially increase the Fund's ability to extend balance of payments assistance to its member countries.

Under the first action, the Executive Board has submitted a resolution to the Board of Governors containing proposals for increases in members' quotas under the Eighth General Review of Quotas in the Fund. If all members accept the increases in their quotas to the proposed amounts, total quotas in the Fund would rise to approximately SDR 90 billion from SDR 61 billion.

Under the second action, the Executive Board has adopted a decision approving a revision and an enlargement of the General Arrangements to Borrow (GAB), which, when it becomes effective, will, inter alia, increase the amount of resources available to the Fund under the GAB from approximately SDR 6.4 billion to SDR 17 billion, and make GAB resources available to finance purchases by any Fund member.

Attached are two separate press releases (Nos. 83/18 and 83/19) containing additional information on the proposals for the Eighth General Review of Quotas and the decision on the General Arrangements to Borrow.

Attachments

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INTERNATIONAL MONETARY FUND

PRESS RELEASE NO. 83/18

FOR IMMEDIATE RELEASE
March 1, 1983

The Executive Board of the International Monetary Fund has submitted a Resolution to the Board of Governors proposing an increase in Fund quotas to approximately SDR 90 billion from SDR 61 billion.

The Governors are to vote on the proposed Resolution, without meeting, by March 31, 1983. The adoption of the Resolution requires a majority of 85 per cent of the total voting power of the Fund's membership.

The Resolution is accompanied by a report of the Executive Board on matters relating to the Eighth General Review of Quotas, and follows agreements reached by the Interim Committee at its meeting on February 10-11, 1983 in Washington, D.C. Annexed to the Resolution are the quotas proposed for each member which were arrived at in the following way:

Forty per cent of the overall increase was distributed to all members in proportion to their present individual quotas, and the balance of 60 per cent was distributed in the form of selective adjustments in proportion to each member's share in the total of the calculated quotas, i.e., the quotas that broadly reflect members' relative positions in the world economy.

Twenty-five per cent of the increase in each member's quota will be paid in SDRs, or in currencies of other members prescribed by the Fund, subject to their concurrence.

The Executive Board also considered the position of the 17 members with very small quotas, i.e., those quotas that are currently less than SDR 10 million. As noted in its report to the Board of Governors, the Executive Board recommends that the quotas of these 17 members shall, after being increased by the method applicable uniformly to all members, be further adjusted to the next higher multiple of SDR 0.5 million. All other quotas would be rounded to the next higher multiple of SDR 0.1 million.

Under the Resolution, members would have until November 30, 1983 to consent to the proposed increases. In order to meet this date members will need to expedite whatever action may be necessary under their laws to enable them to give their consent to the quotas proposed for them. A member's quota cannot be increased until it has consented to the increase and paid the subscription in full. No increase in quota becomes effective before the date of the Fund's determination that members having not less than 70 per cent of present quotas have consented to the increases proposed for them.

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External Relations Department • Washington, D.C. 20431 • Telephone 202-477-3011

The report of the Executive Board to the Board of Governors on the increase in quotas of Fund members under the Eighth General Review, and the Resolution as sent to the Board of Governors with the Annex showing the proposed quotas for all members, are attached.

Attachments

INTERNATIONAL MONETARY FUND

Report of the Executive Directors to the Board of Governors: Increase in Quotas of Fund Members - Eighth General Review

1. Article III, Section 2(a) of the Articles of Agreement provides that "The Board of Governors shall at intervals of not more than five years conduct a general review, and if it deems it appropriate, propose an adjustment of the quotas of the members. It may also, if it thinks fit, consider at any other time the adjustment of any particular quota at the request of the member concerned." This report and the attached Resolution on increases in quotas under the current, i.e., Eighth, General Review are submitted to the Board of Governors in accordance with Article III, Section 2.

2. The Seventh General Review of Quotas was completed by Board of Governors Resolution No. 34-2, adopted December 11, 1978. To comply with the five-year interval prescribed by Article III, Section 2(a), the Eighth General Review has to be completed not later than December 11, 1983. In the Report of the Executive Board to the Board of Governors on Increases in Quotas of Fund Members--Seventh General Review, it was stated that:

> "The Executive Board will review the customary method of calculating quotas after the Seventh Review of Quotas has been completed. In the context of the next general review of quotas, the Executive Board will examine the quota shares of members in relation to their positions in the world economy with a view to adjusting those shares better to reflect members' relative economic positions while having regard to the desirability of an appropriate balance in the composition of the Executive Board."

3. At its meeting in Helsinki, Finland, in May 1982, the Interim Committee urged the Executive Board to pursue its work on the Eighth General Review as a matter of high priority. At that meeting the Committee also "... noting that the present quotas of a significant number of members do not reflect their relative positions in the world economy, ... reaffirmed its view that the occasion of an enlargement of the Fund under the Eighth General Review should be used to bring the quotas of these members more in line with their relative positions, taking account of the case for maintaining a proper balance between the different groups of countries." At its meeting in Toronto, Canada, in September 1982, the Committee noted that "there was widespread support in the Committee on the urgent need for a substantial increase in quotas under the Eighth General Review" and "urged the Executive Board to pursue its work on the issues of the Review as a matter of high priority, so that the remaining issues on the size and distribution of the quota increase could be resolved by the time of the Committee's next meeting in April 1983."

4. In its discussions on the Eighth General Review, the Executive Board has considered, inter alia, (i) the method of calculating quotas; (ii) the size of the overall increase in quotas; (iii) the distribution of the overall increase; (iv) the position of countries with very small quotas in the Fund; and (v) the mode of payment for the increase in quotas.

5. As regards the Executive Board's review of the method of calculating quotas, the Executive Board agreed to certain changes regarding the quota formulas used for calculating quotas in connection with the Eighth General Review. The Executive Board accepted the quota calculations based on the revised quota formulas as reasonable indicators of the relative positions of countries in the world economy, though some Directors felt that they do not provide a wholly satisfactory measure of relative economic positions. It is understood that the changes that have been made do not preclude further appropriate changes in connection with future reviews.

6. At the meeting of the Interim Committee held in Washington in February 1983, which had been advanced from April 1983, agreement was reached on all major issues of the Eighth Review, as reflected in the relevant passages from the Committee's communique of February 11, 1983, as follows:

> "(a) The total of Fund quotas should be increased under the Eighth General Review from approximately SDR 61.03 billion to SDR 90 billion (equivalent to about US$98.5 billion).
>
> (b) Forty per cent of the overall increase should be distributed to all members in proportion to their present individual quotas, and the balance of sixty per cent should be distributed in the form of selective adjustments in proportion to each member's share in the total of the calculated quotas, i.e., the quotas that broadly reflect members' relative positions in the world economy.
>
> (c) Twenty-five per cent of the increase in each member's quota should be paid in SDRs or in usable currencies of other members."

The Committee also considered the possibility of a special adjustment of very small quotas, i.e., those quotas that are currently less than SDR 10 million, and agreed to refer this matter to the Executive Board for urgent consideration in connection with the implementation of the main decision.

7. As requested by the Interim Committee at its meeting on February 11, 1983, the Executive Board has considered the position of the 17 members with very small quotas--i.e., those with quotas that at present are less than SDR 10 million. The Executive Board proposes that the quotas of these members should, after being increased in accordance with (b) quoted

in paragraph 6 above, be further adjusted to the next higher multiple of SDR 0.5 million. The Executive Board proposes that all other quotas be rounded to the next higher multiple of SDR 0.1 million. The rounding to SDR 0.5 million would provide for larger quota increases relative to present quotas for most of the members with very small quotas.

8. In accordance with the agreement reached by the Interim Committee at its meeting on February 11, 1983, on items (a) and (b) quoted in paragraph 6 above and with rounding adjustments indicated in paragraph 7 above, the Executive Board proposes to the Board of Governors that the new quotas of members be as set out in the Annex to the proposed Resolution. These increases would raise Fund quotas from approximately SDR 61 billion to approximately SDR 90 billion.

9. Article III, Section 3(a) provides that 25 per cent of any increase shall be paid in special drawing rights, but permits the Board of Governors to prescribe, inter alia, that this payment may be made on the same basis for all members, in whole or in part in the currencies of other members specified by the Fund, subject to their concurrence. Paragraph 5 of the Resolution provides that 25 per cent of the increase in quotas proposed as a result of the current review should be paid in SDRs or in currencies of other members selected by the Fund, subject to their concurrence, or in any combination of SDRs and such currencies. The balance of the increase shall be paid in a member's own currency. A reserve asset payment will help strengthen the liquidity of the Fund and will not impose an undue burden on members because under the existing decisions of the Fund a reserve asset payment will either enlarge or create a reserve tranche position of an equivalent amount. In addition, the Fund stands ready to assist members that do not hold sufficient reserves to make their reserve asset payments to the Fund to borrow SDRs from other members willing to cooperate; these loans would be made on the condition that such members would repay on the same day the loans from the SDR proceeds of drawings of reserve tranches which had been established by the payment of SDRs.

10. Under the proposed Resolution, a member will be able to consent only to the amount of quota proposed for it in the Annex. A member will be able to consent to the increase in its quota at any time before 6:00 p.m., Washington time, November 30, 1983. In order to meet this time, members will have until the end of November 1983 to complete whatever action may be necessary under their laws to enable them to give their consents.

11. A member's quota cannot be increased until it has consented to the increase and paid the subscription. Under the proposed Resolution, the increase in a member's quota will take effect only after the Fund has received the member's consent to the increase in quota and a member has paid the increase in subscription, provided that the quota cannot become effective before the date on which the Fund determines that the participation requirement in paragraph 2 of the proposed Resolution has been satisfied. The Executive Board is authorized by paragraph 3 of the proposed Resolution to extend the period of consent.

12. The participation requirement in paragraph 2 will be reached when the Fund determines that members having not less than seventy per cent of the total of quotas on February 28, 1983 have consented to the increases in their respective quotas as set out in the Annex.

13. The proposed Resolution provides that a member must pay the increase in its subscription within 30 days after (a) the date on which the member notifies the Fund of its consent, or (b) the date on which the participation requirement is met, whichever is the later.

14. The Executive Board recommends that the Board of Governors adopt the attached Resolution that covers all the matters on which the Governors are requested to act. The adoption of the Resolution requires positive responses from Governors having an 85 per cent majority of the total voting power.

Attachment

Proposed Resolution of the Board of Governors:
Increase in Quotas of Fund Members--Eighth General Review

WHEREAS the Executive Board has submitted to the Board of Governors a report entitled "Increases in Quotas of Fund Members--Eighth General Review" containing recommendations on increases in the quotas of individual members of the Fund; and

WHEREAS the Executive Board has recommended the adoption of the following Resolution of the Board of Governors, which Resolution proposes increases in the quotas of members of the Fund as a result of the Eighth General Review of Quotas and deals with certain related matters, by vote without meeting pursuant to Section 13 of the By-Laws of the Fund;

NOW, THEREFORE, the Board of Governors hereby RESOLVES that:

1. The International Monetary Fund proposes that, subject to the provisions of this Resolution, the quotas of members of the Fund shall be increased to the amounts shown against their names in the Annex to this Resolution.

2. A member's increase in quota as proposed by this Resolution shall not become effective unless the member has notified the Fund of its consent to the increase not later than the date prescribed by or under paragraph 3 below and has paid the increase in quota in full, provided that no increase in quota shall become effective before the date of the Fund's determination that members having not less than 70 per cent of the total of quotas on February 28, 1983 have consented to the increases in their quotas.

3. Notices in accordance with paragraph 2 above shall be executed by a duly authorized official of the member and must be received in the Fund before 6:00 p.m., Washington time, November 30, 1983, provided that the Executive Board may extend this period as it may determine.

4. Each member shall pay to the Fund the increase in its quota within 30 days after the later of (a) the date on which it notifies the Fund of its consent, or (b) the date of the Fund's determination under paragraph 2 above.

5. Each member shall pay twenty-five per cent of its increase either in special drawing rights or in the currencies of other members specified, with their concurrence, by the Fund, or in any combination of special drawing rights and such currencies. The balance of the increase shall be paid by the member in its own currency.

		Proposed Quota (In millions of SDRs)
1.	Afghanistan	86.7
2.	Algeria	623.1
3.	Antigua and Barbuda	5.0
4.	Argentina	1,113.0
5.	Australia	1,619.2
6.	Austria	775.6
7.	Bahamas	66.4
8.	Bahrain	48.9
9.	Bangladesh	287.5
10.	Barbados	34.1
11.	Belgium	2,080.4
12.	Belize	9.5
13.	Benin	31.3
14.	Bhutan	2.5
15.	Bolivia	90.7
16.	Botswana	22.1
17.	Brazil	1,461.3
18.	Burma	137.0
19.	Burundi	42.7
20.	Cameroon	92.7
21.	Canada	2,941.0
22.	Cape Verde	4.5
23.	Central African Republic	30.4
24.	Chad	30.6
25.	Chile	440.5
26.	China	2,390.9
27.	Colombia	394.2
28.	Comoros	4.5
29.	Congo, People's Republic	37.3
30.	Costa Rica	84.1
31.	Cyprus	69.7
32.	Denmark	711.0
33.	Djibouti	8.0
34.	Dominica	4.0
35.	Dominican Republic	112.1
36.	Ecuador	150.7
37.	Egypt	463.4
38.	El Salvador	89.0
39.	Equatorial Guinea	18.4
40.	Ethiopia	70.6

		Proposed Quota (In millions of SDRs)
41.	Fiji	36.5
42.	Finland	574.9
43.	France	4,482.8
44.	Gabon	73.1
45.	Gambia, The	17.1
46.	Germany	5,403.7
47.	Ghana	204.5
48.	Greece	399.9
49.	Grenada	6.0
50.	Guatemala	108.0
51.	Guinea	57.9
52.	Guinea-Bissau	7.5
53.	Guyana	49.2
54.	Haiti	44.1
55.	Honduras	67.8
56.	Hungary	530.7
57.	Iceland	59.6
58.	India	2,207.7
59.	Indonesia	1,009.7
60.	Iran, Islamic Republic of	1,117.4
61.	Iraq	504.0
62.	Ireland	343.4
63.	Israel	446.6
64.	Italy	2,909.1
65.	Ivory Coast	165.5
66.	Jamaica	145.5
67.	Japan	4,223.3
68.	Jordan	73.9
69.	Kampuchea, Democratic	25.0
70.	Kenya	142.0
71.	Korea	462.8
72.	Kuwait	635.3
73.	Lao People's Democratic Republic	29.3
74.	Lebanon	78.7
75.	Lesotho	15.1
76.	Liberia	71.3
77.	Libya	515.7
78.	Luxembourg	77.0
79.	Madagascar	66.4
80.	Malawi	37.2

		Proposed Quota (In millions of SDRs)
81.	Malaysia	550.6
82.	Maldives	2.0
83.	Mali	50.8
84.	Malta	45.1
85.	Mauritania	33.9
86.	Mauritius	53.6
87.	Mexico	1,165.5
88.	Morocco	306.6
89.	Nepal	37.3
90.	Netherlands	2,264.8
91.	New Zealand	461.6
92.	Nicaragua	68.2
93.	Niger	33.7
94.	Nigeria	849.5
95.	Norway	699.0
96.	Oman	63.1
97.	Pakistan	546.3
98.	Panama	102.2
99.	Papua New Guinea	65.9
100.	Paraguay	48.4
101.	Peru	330.9
102.	Philippines	440.4
103.	Portugal	376.6
104.	Qatar	114.9
105.	Romania	523.4
106.	Rwanda	43.8
107.	St. Lucia	7.5
108.	St. Vincent	4.0
109.	Sao Tome & Principe	4.0
110.	Saudi Arabia	3,202.4
111.	Senegal	85.1
112.	Seychelles	3.0
113.	Sierra Leone	57.9
114.	Singapore	250.2
115.	Solomon Islands	5.0
116.	Somalia	44.2
117.	South Africa	915.7
118.	Spain	1,286.0
119.	Sri Lanka	223.1
120.	Sudan	169.7

		Proposed Quota (In millions of SDRs)
121.	Suriname	49.3
122.	Swaziland	24.7
123.	Sweden	1,064.3
124.	Syrian Arab Republic	139.1
125.	Tanzania	107.0
126.	Thailand	386.6
127.	Togo	38.4
128.	Trinidad and Tobago	170.1
129.	Tunisia	138.2
130.	Turkey	429.1
131.	Uganda	99.6
132.	United Arab Emirates	385.9
133.	United Kingdom	6,194.0
134.	United States	17,918.3
135.	Upper Volta	31.6
136.	Uruguay	163.8
137.	Vanuatu	9.0
138.	Venezuela	1,371.5
139.	Viet Nam	176.8
140.	Western Samoa	6.0
141.	Yemen Arab Republic	43.3
142.	Yemen, People's Democratic Republic of	77.2
143.	Yugoslavia	613.0
144.	Zaire	291.0
145.	Zambia	270.3
146.	Zimbabwe	191.0

INTERNATIONAL MONETARY FUND

PRESS RELEASE NO. 83/19

FOR IMMEDIATE RELEASE
March 1, 1983

The Executive Board of the International Monetary Fund has completed the work necessary to enable a revision and enlargement of the General Arrangements to Borrow (GAB), which had recently been agreed in principle by the Group of Ten and the Fund. The main change is a substantial increase to SDR 17 billion in the credit arrangements available to the Fund from the present size of approximately SDR 6.4 billion. Other amendments to the existing GAB provisions will (i) permit the Fund to borrow under the enlarged credit arrangements to finance exchange transactions with members that are not GAB participants, (ii) authorize Swiss participation and (iii) permit certain borrowing arrangements between the Fund and non-participating members to be associated with the GAB, with the possibility that the Fund could activate the GAB as if the associated lenders were GAB participants.

The changes will become effective when all ten participants--Belgium, Canada, Deutsche Bundesbank, France, Italy, Japan, Netherlands, Sveriges Riksbank, United Kingdom and the United States--have notified the Fund in writing that they concur in the amendments and in the increased credit commitments. Participants are asked to do so by December 31, 1983. Swiss participation will become effective when the amended decision has become effective.

Under the GAB, which became effective on October 24, 1962, ten industrial members extended credit lines to the Fund. The arrangements have been periodically renewed, with some modifications, and in one case, that of Japan, the original amount of the credit line has been increased.

The Fund will continue to be able to call on GAB resources for any drawings by participants when supplementary resources are needed to forestall or cope with an impairment of the international monetary system. As soon as the revision to the GAB becomes effective, the Fund may also call on GAB resources to finance drawings by Fund members that are not partipants provided those transactions are made under policies of the Fund requiring adjustment programs. Calls on the GAB will be made, in respect of non-participants, if the Fund faces an inadequacy of resources to meet actual and expected requests for financing that reflect the existence of an exceptional situation associated with balance of payments problems of members that would threaten the stability of the international monetary system.

The revised decision on the GAB and an annex showing the participants and amounts of credit arrangements under both the existing and the future GAB are attached.

Attachment

ATTACHMENT

GENERAL ARRANGEMENTS TO BORROW

Preamble

In order to enable the International Monetary Fund to fulfill more effectively its role in the international monetary system, the main industrial countries have agreed that they will, in a spirit of broad and willing cooperation, strengthen the Fund by general arrangements under which they will stand ready to make loans to the Fund up to specified amounts under Article VII, Section 1 of the Articles of Agreement when supplementary resources are needed to forestall or cope with an impairment of the international monetary system. In order to give effect to these intentions, the following terms and conditions are adopted under Article VII, Section 1 of the Articles of Agreement.

Paragraph 1. Definitions

As used in this Decision the term:

(i) "Articles" means the Articles of Agreement of the International Monetary Fund;

(ii) "credit arrangement" means an undertaking to lend to the Fund on the terms and conditions of this Decision;

(iii) "participant" means a participating member or a participating institution;

(iv) "participating institution" means an official institution of a member that has entered into a credit arrangement with the Fund with the consent of the member;

(v) "participating member" means a member of the Fund that has entered into a credit arrangement with the Fund;

(vi) "amount of a credit arrangement" means the maximum amount expressed in special drawing rights that a participant undertakes to lend to the Fund under a credit arrangement;

(vii) "call" means a notice by the Fund to a participant to make a transfer under its credit arrangement to the Fund's account;

(viii) "borrowed currency" means currency transferred to the Fund's aecount under a credit arrangement;

(ix) "drawer" means a member that purchases borrowed currency from the Fund in an exchange transaction or in an exchange transaction under a stand-by or extended arrangement;

(x) "indebtedness" of the Fund means the amount it is committed to repay under a credit arrangement.

Paragraph 2. Credit Arrangements

A member or institution that adheres to this Decision undertakes to lend its currency to the Fund on the terms and conditions of this Decision up to the amount in special drawing rights set forth in the Annex to this Decision or established in accordance with Paragraph 3(b).

Paragraph 3. Adherence

(a) Any member or institution specified in the Annex may adhere to this Decision in accordance with Paragraph 3(c).

(b) Any member or institution not specified in the Annex that wishes to become a participant may at any time, after consultation with the Fund, give notice of its willingness to adhere to this Decision, and, if the Fund shall so agree and no participant object, the member or institution may adhere in accordance with Paragraph 3(c). When giving notice of its willingness to adhere under this Paragraph 3(b) a member or institution shall specify the amount, expressed in terms of the special drawing right, of the credit arrangement which it is willing to enter into, provided that the amount shall not be less than the amount of the credit arrangement of the participant with the smallest credit arraagement.

(c) A member or institution shall adhere to this Decision by depositing with the Fund an instrument setting forth that it has adhered in accordance with its law and has taken all steps necessary to enable it to carry out the terms and conditions of this Decision. On the deposit of the instrument the member or institution shall be a participant as of the date of the deposit or of the effective date of this Decision, whichever shall be later.

Paragraph 4. Entry into Force

This Decision shall become effective when it has been adhered to by at least seven of the members or institutions included in the Annex with credit arrangements amounting in all to not less than the equivalent of five and one-half billion United States dollars of the weight and fineness in effect on July 1, 1944.

Paragraph 5. Changes in Amounts of Credit Arrangements

The amounts of participants' credit arrangements may be reviewed from time to time in the light of developing circumstances and changed with the agreement of the Fund and all participants.

Paragraph 6. Initial Procedure

When a participating member or a member whose institution is a participant approaches the Fund on an exchange transaction or stand-by or extended arrangement and the Managing Director, after consultation, considers that the exchange transaction or stand-by or extended arrangement is necessary in order to forestall or cope with an impairment of the international monetary system, and that the Fund's resources need to be supplemented for this purpose, he shall initiate the procedure for making calls under Paragraph 7.

Paragraph 7. Calls

(a) The Managing Director shall make a proposal for calls for an exchange transaction or for future calls for exchange transactions under a stand-by or extended arrangement only after consultation with Executive Directors and participants. A proposal shall become effective only if it is accepted by participants and the proposal is then approved by the Executive Board. Each participant shall notify the Fund of the acceptance of a proposal involving a call under its credit arrangement.

(b) The currencies and amounts to be called under one or more of the credit arrangements shall be based on the present and prospective balance of payments and reserve position of participating members or members whose institutions are participants and on the Fund's holdings of currencies.

(c) Unless otherwise provided in a proposal for future calls approved under Paragraph 7(a), purchases of borrowed currency under a stand-by or extended arrangement shall be made in the currencies of participants in proportion to the amounts in the proposal.

(d) If a participant on which calls may be made pursuant to Paragraph 7(a) for a drawer's purchases under a stand-by or extended arrangement gives notice to the Fund that in the participant's opinion, based on the present and prospective balance of payments and reserve position, calls should no longer be made on the participant or that calls should be for a smaller amount, the Managing Director may propose to other participants that substitute amounts be made available under their credit arrangements, and this proposal shall be subject to the procedure of Paragraph 7(a). The proposal as originally approved under Paragraph 7(a) shall remain effective unless and until a proposal for substitute amounts is approved in accordance with Paragraph 7(a).

(e) When the Fund makes a call pursuant to this Paragraph 7, the participant shall promptly make the transfer in accordance with the call.

Paragraph 8. Evidence of Indebtedness

(a) The Fund shall issue to a participant, on its request, non-negotiable instruments evidencing the Fund's indebtedness to the participant. The form of the instruments shall be agreed between the Fund and the participant.

(b) Upon repayment of the amount of any instrument issued under Paragraph 8(a) and all accrued interest, the instrument shall be returned to the Fund for cancellation. If less than the amount of any such instrument is repaid, the instrument shall be returned to the Fund and a new instrument for the remainder of the amount shall be substituted with the same maturity date as in the old instrument.

Paragraph 9. Interest

(a) The Fund shall pay interest on its indebtedness at a rate equal to the combined market interest rate computed by the Fund from time to time for the purpose of determining the rate at which it pays interest on holdings of special drawing rights. A change in the method of calculating the combined market interest rate shall apply only if the Fund and at least two thirds of the participants having three fifths of the total amount of the credit arrangements so agree; provided that if a participant so requests at the time this agreement is reached, the change shall not apply to the Fund's indebtedness to that participant outstanding at the date the change becomes effective.

(b) Interest shall accrue daily and shall be paid as soon as possible after each July 31, October 31, January 31, and April 30.

(c) Interest due to a participant shall be paid, as determined by the Fund, in special drawing rights, or in the participant's currency, or in other currencies that are actually convertible.

Paragraph 10. Use of Borrowed Currency

The Fund's policies and practices under Article V, Sections 3 and 7 on the use of its general resources and stand-by and extended arrangements, including those relating to the period of use, shall apply to purchases of currency borrowed by the Fund. Nothing in this Decision shall affect the authority of the Fund with respect to requests for the use of its resources by individual members, and access to these resources by members shall be determined by the Fund's policies and practices, and shall not depend on whether the Fund can borrow under this Decision.

Paragraph 11. Repayment by the Fund

(a) Subject to the other provisions of this Paragraph 11, the Fund, five years after a transfer by a participant, shall repay the participant an amount equivalent to the transfer calculated in accordance with Paragraph 12. If the drawer for whose purchase participants make transfers is committed to repurchase at a fixed date earlier than five years after its purchase, the Fund shall repay the participants at that date. Repayment under this Paragraph 11(a) or under Paragraph 11(c) shall be, as determined by the Fund, in the participant's currency whenever feasible, or in special drawing rights, or, after consultation with the participant, in other currencies that are actually convertible. Repayments to a participant under Paragraph 11(b) and (e) shall be credited against transfers by the participant for a drawer's purchases in the order in which repayment must be made under this Paragraph 11(a).

(b) Before the date prescribed in Paragraph 11(a), the Fund, after consultation with a participant, may make repayment to the participant in part or in full. The Fund shall have the option to make repayment under this Paragraph 11(b) in the participant's currency, or in special drawing rights in an amount that does not increase the participant's holdings of special drawing rights above the limit under Article XIX, Section 4, of the Articles of Agreement unless the participant agrees to accept special drawing rights above that limit in such repayment, or, with the agreement of the participant, in other currencies that are actually convertible.

(c) Whenever a reduction in the Fund's holdings of a drawer's currency is attributed to a purchase of borrowed currency, the Fund shall promptly repay an equivalent amount. If the Fund is indebted to a participant as a result of transfers to finance a reserve tranche purchase by a drawer and the Fund's holdings of the drawer's currency that are not subject to repurchase are reduced as a result of net sales of that currency during a quarterly period covered by an operational budget, the Fund shall repay at the beginning of the next quarterly period an amount equivalent to that reduction, up to the amount of the indebtedness to the participant.

(d) Repayment under Paragraph 11(c) shall be made in proportion to the Fund's indebtedness to the participants that made transfers in respect of which repayment is being made.

(e) Before the date prescribed in Paragraph 11(a) a participant may give notice representing that there is a balance of payments need for repayment of part or all of the Fund's indebtedness and requesting such repayment. The Fund shall give the overwhelming benefit of any doubt to the participant's representation. Repayment shall be made after consultation with the participant in the currencies of other members that are actually convertible, or made in special drawing rights, as determined by the Fund. If the Fund's holdings of currencies in which repayment should be made are not wholly adequate, individual participants shall be requested, and will be expected, to provide the necessary balance under their credit arrangements. If, notwithstanding the expectation that the participants will provide the necessary balance, they fail to do so, repayment shall be made to the extent necessary in the currency of the drawer for whose purchases the participant requesting repayment made transfers. For all of the purposes of this Paragraph 11 transfers under this Paragraph 11(e) shall be deemed to have been made at the same time and for the same purchases as the transfers by the participant obtaining repayment under this Paragraph 11(e).

(f) All repayments to a participant in a currency other than its own shall be guided, to the maximum extent practicable, by the present and prospective balance of payments and reserve position of the members whose currencies are to be used in repayment.

(g) The Fund shall at no time reduce its holdings of a drawer's currency below an amount equal to the Fund's indebtedness to the participants resulting from transfers for the drawer's purchases.

(h) When any repayment is made to a participant, the amount that can be called for under its credit arrangement in accordance with this Decision shall be restored pro tanto.

(i) The Fund shall be deemed to have discharged its obligations to a participating institution to make repayment in accordance with the provisions of this Paragraph or to pay interest in accordance with the provisions of Paragraph 9 if the Fund transfers an equivalent amount in special drawing rights to the member in which the institution is established.

Paragraph 12. Rates of Exchange

(a) The value of any transfer shall be calculated as of the date of the dispatch of the instructions for the transfer. The calculation shall be made in terms of the special drawing right in accordance with Article XIX, Section 7(a) of the Articles, and the Fund shall be obliged to repay an equivalent value.

(b) For all of the purposes of this Decision, the value of a currency in terms of the special drawing right shall be calculated by the Fund in accordance with Rule O-2 of the Fund's Rules and Regulations.

Paragraph 13. Transferability

A participant may not transfer all or part of its claim to repayment under a credit arrangement except with the prior consent of the Fund and on such terms and conditions as the Fund may approve.

Paragraph 14. Notices

Notice to or by a participating member under this Decision shall be in writing or by rapid means of communication and shall be given to or by the fiscal agency of the participating member designated in accordance with Article V, Section 1 of the Articles and Rule G-1 of the Rules and Regulations of the Fund. Notice to or by a participating institution shall be in writing or by rapid means of communication and shall be given to or by the participating institution.

Paragraph 15. Amendment

This Decision may be amended during the period prescribed in Paragraph 19(a) only by a decision of the Fund and with the concurrence of all participants. Such concurrence shall not be necessary for the modification of the Decision on its renewal pursuant to Paragraph 19(b).

Paragraph 16. Withdrawal of Adherence

A participant may withdraw its adherence to this Decision in accordance with Paragraph 19(b) but may not withdraw within the period prescribed in Paragraph 19(a) except with the agreement of the Fund and all participants.

Paragraph 17. Withdrawal from Membership

If a participating member or a member whose institution is a participant withdraws from membership in the Fund, the participant's credit arrangement shall cease at the same time as the withdrawal takes effect. The Fund's indebtedness under the credit arrangement shall be treated as an amount due from the Fund for the purpose of Article XXVI, Section 3, and Schedule J of the Articles.

Paragraph 18. Suspension of Exchange Transactions and Liquidation

(a) The right of the Fund to make calls under Paragraph 7 and the obligation to make repayments under Paragraph 11 shall be suspended during any suspension of exchange transactions under Article XXVII of the Articles.

(b) In the event of liquidation of the Fund, credit arrangements shall cease and the Fund's indebtedness shall constitute liabilities under Schedule K of the Articles. For the purpose of Paragraph 1(a) of Schedule K, the currency in which the liability of the Fund shall be payable shall be first the participant's currency and then the currency of the drawer for whose purchases transfers were made by the participants.

Paragraph 19. Period and Renewal

(a) This Decision shall continue in existence for four years from its effective date. A new period of five years shall begin on the effective date of Decision No. 7337-(83/37), adopted February 24, 1983. References in Paragraph 19(b) to the period prescribed in Paragraph 19(a) shall refer to this new period and to any subsequent renewal periods that may be decided pursuant to Paragraph 19(b). When considering a renewal of this Decision for the period following the five-year period referred to in this Paragraph 19(a), the Fund and the participants shall review the functioning of this Decision, including the provisions of Paragraph 21.

(b) This Decision may be renewed for such period or periods and with such modifications, subject to Paragraph 5, as the Fund may decide. The Fund shall adopt a decision on renewal and modification, if any, not later than twelve months before the end of the period prescribed in Paragraph 19(a). Any participant may advise the Fund not less than six months before the end of the period prescribed in Paragraph 19(a) that it will withdraw its adherence to the Decision as renewed. In the absence of such notice, a participant shall be deemed to continue to adhere to the Decision as renewed. Withdrawal of adherence in accordance with this Paragraph 19(b) by a participant, whether or not included in the Annex, shall not preclude its subsequent adherence in accordance with Paragraph 3(b).

(c) If this Decision is terminated or not renewed, Paragraph 8 through 14, 17 and 18(b) shall nevertheless continue to apply in connection with any indebtedness of the Fund under credit arrangements in existence at the date of the termination or expiration of the Decision until repayment is completed. If a participant withdraws its adherence to this Decision in accordance with Paragraph 16 or Paragraph 19(b), it shall cease to be a participant under the Decision, but Paragraphs 8 through 14, 17 and 18(b) of the Decision as of the date of the withdrawal shall nevertheless continue to apply to any indebtedness of the Fund under the former credit arrangement until repayment has been completed.

Paragraph 20. Interpretation

Any question of interpretation raised in connection with this Decision which does not fall within the purview of Article XXIX of the Articles shall be settled to the mutual satisfaction of the Fund, the participant raising the question, and all other participants. For the purpose of this Paragraph 20 participants shall be deemed to include those former participants to which Paragraphs 8 through 14, 17 and 18(b) continue to apply pursuant to Paragraph 19(c) to the extent that any such former participant is affected by a question of interpretation that is raised.

Paragraph 21. Use of Credit Arrangements for Nonparticipants

(a) The Fund may make calls in accordance with Paragraphs 6 and 7 for exchange transactions requested by members that are not participants if the exchange transactions are (i) transactions in the upper credit tranches, (ii) transactions under stand-by arrangements extending beyond the first credit tranche, (iii) transactions under extended arrangements, or (iv) transactions in the first credit tranche in conjunction with a stand-by or an extended arrangement. All the provisions of this Decision relating to calls shall apply, except as otherwise provided in Paragraph 21(b).

(b) The Managing Director may initiate the procedure for making calls under Paragraph 7 in connection with requests referred to in Paragraph 21(a) if, after consultation, he considers that the Fund faces an inadequacy of resources to meet actual and expected requests for financing that reflect the existence of an exceptional situation associated with balance of payments problems of members of a character or aggregate size that could threaten the stability of the international monetary system. In making proposals for calls pursuant to Paragraph 21(a) and (b), the Managing Director shall pay due regard to potential calls pursuant to other provisions of this Decision.

Paragraph 22. Participation of the Swiss National Bank

(a) Notwithstanding any other provision of this Decision, the

Swiss National Bank (hereinafter called the Bank) may become a participant by adhering to this Decision in accordance with Paragraph 3(c) and accepting, by its adherence, a credit arrangement in an amount equivalent to one thousand and twenty million special drawing rights. Upon adherence, the Bank shall be deemed to be a participating institution, and all the provisions of this Decision relating to participating institutions shall apply in respect of the Bank, subject to, and as supplemented by, Paragraph 22(b), (c), (d), (e), and (f).

(b) Under its credit arrangement, the Bank undertakes to lend any currency, specified by the Managing Director after consultation with the Bank at the time of a call, that the Fund has determined to be a freely usable currency pursuant to Article XXX(f) of the Articles.

(c) In relation to the Bank, the references to the balance of payments and reserve position in Paragraph 7(b) and (d), and Paragraph 11(e), shall be understood to refer to the position of the Swiss Confederation.

(d) In relation to the Bank, the references to a participant's currency in Paragraph 9(c), Paragraph 11(a) and (b), and Paragraph 18(b) shall be understood to refer to any currency, specified by the Managing Director after consultation with the Bank at the time of payment by the Fund, that the Fund has determined to be a freely usable currency pursuant to Article XXX(f) of the Articles.

(e) Payment of special drawing rights to the Bank pursuant to Paragraph 9(c) and Paragraph 11 shall be made only while the Bank is a prescribed holder pursuant to Article XVII of the Articles.

(f) The Bank shall accept as binding a decision of the Fund on any question of interpretation raised in connection with this Decision which falls within the purview of Article XXIX of the Articles, to the same extent as that decision is binding on other participants.

Paragraph 23. Associated Borrowing Arrangements

(a) A borrowing arrangement between the Fund and a member that is not a participant, or an official institution of such a member, under which the member or the official institution undertakes to make loans to the Fund for the same purposes as, and on terms comparable to, those made by participants under this Decision, may, with the concurrence of all participants, authorize the Fund to make calls on participants in accordance with Paragraphs 6 and 7 for exchange transactions with that member, or to make requests under Paragraph 11(e) in connection with an early repayment of a claim under the borrowing arrangement, or both. For the purposes of this Decision such calls or requests shall be treated as if they were calls or requests in respect of a participant.

(b) Nothing in this Decision shall preclude the Fund from entering into any other types of borrowing arrangements, including an arrangement between the Fund and a lender, involving an association with participants, that does not contain the authorizations referred to in Paragraph 23(a).

ANNEX

Participants and Amounts of Credit Arrangements

I. Prior to the Effective Date of Decision No. 7337-(83/37)

Participant			Amount in Units of Participant's currency
1.	United States of America	US$	2,000,000,000
2.	Deutsche Bundesbank	DM	4,000,000,000
3.	United Kingdom	£	357,142,857
4.	France	F	2,715,381,428
5.	Italy	Lit	343,750,000,000
6.	Japan	Yen	340,000,000,000
7.	Canada	Can$	216,216,000
8.	Netherlands	f.	724,000,000
9.	Belgium	BF	7,500,000,000
10.	Sveriges Riksbank	SKr	517,320,000

II. From the Effective Date of Decision No. 7337-(83/37)

Participant		Amount in special drawing rights
1.	United States of America	4,250,000,000
2.	Deutsche Bundesbank	2,380,000,000
3.	Japan	2,125,000,000
4.	France	1,700,000,000
5.	United Kingdom	1,700,000,000
6.	Italy	1,105,000,000
7.	Canada	892,500,000
8.	Netherlands	850,000,000
9.	Belgium	595,000,000
10.	Sveriges Riksbank	382,500,000
11.	Swiss National Bank*	1,020,000,000
		17,000,000,000

*With effect from the date on which the Swiss National Bank adheres to this Decision in accordance with Paragraph 22.

IMF Drawings by the United States

The United States has drawn on the International Monetary Fund (IMF) on twenty-four occasions over the past 19 years for a total of about SDR 5.8 billion (equivalent to about $6.5 billion at the exchange rates prevailing at the time of each drawing), the second largest amount of cumulative drawings of any IMF member. None of these drawings was subject to IMF policy conditionality, as they all involved drawings on the U.S. reserve position in the IMF. Drawings on the reserve position are available automatically upon representation of balance of payments need; do not bear interest and are not subject to repurchase obligations; and do not involve policy conditionality.

The U.S. drawings were for the following purposes: during the 1960s and early 1970s they were designed to limit foreign purchases of U.S. gold reserves; subsequently, they were designed to provide the United States with foreign currencies for the purpose of exchange market operations. These purposes are explained below. A table listing all U.S. drawings is attached.

Drawings During the 1960s and 1970s

Under the international monetary arrangements in operation following World War II, each member of the IMF was required to establish and maintain a "par value" for its currency in terms of gold. The United States undertook to fulfill its par value obligations by standing ready to convert dollars held by foreign monetary authorities into gold at the official price of $35 per ounce -- i.e., the par value of the dollar. Other countries met their par value obligations by maintaining exchange rates for their currencies -- directly or indirectly -- in terms of the dollar within narrow margins. In this manner, a strucuture of currency exchange rates linked to gold was established and maintained.

During the 1950s and 1960s, large payments imbalances, substantial losses of U.S. gold and foreign accumulations of dollar holdings, representing further potential strains on U.S. gold, put increasing strain on this system. Beginning in the early 1960s the United States, in cooperation with foreign monetary authorities, initiated a variety of measures designed to limit pressures on U.S. gold holdings. U.S. drawings on the IMF were an integral part of this program.

In general, IMF drawings provided the United States with foreign currencies that could be used to purchase dollars from foreign monetary authorities and thus reduce demands for conversion of official dollar holdings to gold. The foreign currencies obtained from the IMF were used most often in the following types of transactions:

-- to facilitate repayment of IMF drawings by other countries without necessitating the use of U.S. gold;

-- repayment of U.S. short-term currency swaps with foreign central banks; and

-- direct purchases by the United States of foreign official dollar holdings that would otherwise be used to purchase U.S. gold.

Drawings Since the Early 1970s

With the end of the par value/gold convertibility arrangements in the early 1970s, the basic purpose of U.S. drawings from the IMF was to finance U.S. intervention in the exchange markets in support of the dollar. During the 1970s, the U.S. intervened directly in the foreign exchange market, buying and selling foreign currencies for dollars, in order to deal with exchange market pressures on the dollar. The foreign currencies obtained from U.S. drawings in the IMF provided an important source of funds for such intervention. In November 1978, a U.S. drawing of $3 billion of German marks and Japanese yen was a component of a major program of U.S. and foreign intervention in the exchange market to support the dollar.

IMF Drawings by the United States
(SDR Millions)

Date		Amount
1964:	Feb	125
	June	125
	Sept	150
	Dec	125
	Total	525
1965	March	75
	July	300
	Sept	60
	Total	435
1966	Jan	100
	March	60
	April	30
	May	30
	July	71
	Aug	282
	Sept	35
	Oct	31
	Nov	12
	Dec	30
	Total	681
1968:	March	200
	Total	200
1970:	May	150
	Total	150
1971:	Jan	250
	June	250
	Aug	862
	Total	1,362
1972:	April	200
	Total	200
1978:	Nov	2,275
	Total	2,275
Grand Total		5,828 1/

1/ Equivalent to about $6.5 billion at exchange rates prevailing at the time of each drawing.

Budgetary and Financing Impact of Transactions with the IMF under the U.S. Quota in the IMF and U.S. Loans to the IMF

Under budget and accounting procedures established in consultation with the Congress at the time of the 1980 increase in the U.S. IMF quota, an increase in the U.S. quota or line of credit to the IMF requires budget authorization and appropriation for the full amount of increases in the quota or U.S. lending arrangements. The sum is included in the budget authority totals for the fiscal year requested. Payment to the IMF of the increased quota subscription is made partly (25 percent) in reserve assets (SDRs or foreign currencies) and partly in non-interest bearing letters of credit, which are a contingent liability. Under the credit lines established pursuant to IMF borrowing arrangements with the United States, the Treasury is committed to provide funds upon call by the IMF.

A budget expenditure occurs only as cash is actually transferred to the IMF, through the 25 percent reserve asset payment, through encashment of the quota letter of credit, or against the borrowing arrangements. Simultaneous with such transfers, the U.S. receives an equal offsetting receipt, representing an increase in the U.S. reserve position in the IMF -- an interest-bearing, liquid international monetary asset that is available unconditionally to the United States in case of balance of payments need. As a consequence of these offsetting transactions, transfers to the IMF under the quota subscription or U.S. lending arrangements therefore do not result in net budget outlays, or directly affect the budget deficit. Similarly, payments of dollars by the IMF to the United States (for example, resulting from repayments by other IMF member countries) do not result in net budget receipts since the U.S. reserve position declines simultaneously by a like amount.

Transfers from the United States to the IMF under the U.S. quota or U.S. lending arrangements increase Treasury borrowing requirements, while transfers from the IMF to the United States improve the Treasury's cash position and reduce its borrowing requirement. The net effect of transfers to and from the IMF has varied widely over the years, resulting in cash outflows from the Treasury in some years and inflows to the Treasury in other years. Moreover, Treasury interest costs on borrowings to finance any net transfers to the IMF need to be balanced against the remuneration (interest) earned on the U.S. reserve position in the IMF. Finally, the U.S. may incur exchange gains and losses on the U.S. reserve position in the IMF due to changes in the dollar value of the SDR.

It is not possible to project the effect on Treasury borrowing requirements or the net cost of U.S. transactions with the IMF because of uncertainties regarding the future level of IMF financing; the portion of such financing that would be in dollars; and movements in market interest and exchange rates. However, the figures in the attached table indicate that for the period from July 1, 1969, to the end of 1982:

-- Net increases in Treasury borrowing requirements attributable to transactions with the IMF averaged $498 million annually, compared to average annual increases in Treasury borrowing of $61 billion.

-- Treasury debt outstanding attributable to transactions with the IMF averaged $1.9 billlion annually. This is not an annual increase in Treasury borrowing, but an estimate of the average total debt outstanding each year attributable to cumulative U.S. transactions with the IMF. During fiscal 1982, the average outstanding Treasury borrowing attributable to such transactions amounted to $5.3 billion, about 1/2 of 1 percent of the total outstanding Treasury debt of $1.1 trillion at the end of the fiscal year.

-- Net interest costs to the Treasury associated with all U.S. transactions with the IMF averaged $45 million annually. In fiscal 1982, interest costs on total Treasury debt amounted to $117 billion.

-- Net annual valuation losses to the U.S. on the U.S. reserve position in the IMF averaged $62 million.

-- The overall net annual cost to the U.S., taking account of interest and valuation, thus averaged $107 million.

Revised to U.S.
Fiscal Year Basis
March 4, 1983

Estimated Public Debt, Servicing Costs and Budgetary Effects Associated With U.S. Transactions Under U.S. Quota and U.S. Loans to IMF, FY 1970-1983I

(millions of dollars)

TABLE 1

ing U.S. cal Year	Average Outstanding Net Treasury Debt(-) or Cash(+) Position Arising From: Transactions Under U.S. Quota 1/ (1)	U. S. Loans to IMF 2/ (2)	Total 3/ (3)	Est. Treasury Borrowing Cost(-) or Reduction(+) from Column(3) 4/ (4)	Interest Received by U.S. on Loans to IMF 5/ (5)	Remuneration Received by U.S. from IMF 6/ (6)	Valuation Gains(+) or Losses(-) on U.S. Reserve Position 7/ (7)	Interest Earned on Holdings of Foreign Currencies Drawn from IMF 8/ (8)	Total Estimated Net Budgetary Receipts(+) or Outlays(-) 9/ (9)
70	-860	-	-860	-66	-	+13	-	-	-53
71	-571	-	-571	-28	-	+12	-	-	-16
72	+631	-	+631	+26	-	*	+34	-	+60
1973	+801	-	+801	+42	-	-	-	-	+42
1974	+627	-	+627	+50	-	-	+54	-	+104
1975	-481	-	-481	-32	-	*	+48	-	+16
1976	-1,131	-	-1,131	-63	-	+9	-168	-	-222
TQ	-2,467	-	-2,467	-32	-	-	+39	-	+7
1977	-2,973	-379	-3,352	-164	+14	+79	+27	-	-44
1978	-2,314	-663	-2,977	-196	+31	+80	+369	-	+284
1979	-834	-64	-898	-83	+12	+27	+212	+48	+216
1980	-609	-94	-703	-78	*	-	-13	+40	-51
1981	-2,183	-559	-2,742	-376	+46	+22	-1,295	+69	-1,534
1982	-4,233	-1,036	-5,269	-619	+122	+216	-323	+76	-528
1983I	-5,464	-1,308	-6,772	-134	-	+222 10/	+173	+15	+276
tal Period: 1/69-12/31/82				-1,753	+225	+680	-843	+248	-1,443
nual Average	-1,634	-304	-1,938	-130	+17	+50	-62	+18	-107

Footnotes to Table 1

*Indicates less than $500,000.

Estimate of average outstanding Treasury debt or cash position during period arising from U.S. transfers of dollars to the IMF (i.e., an outflow of dollars from Treasury) and dollar balances received by the U.S. from the IMF and from sales of foreign currency drawn by the U.S. from the IMF (i.e., an inflow of dollars to the Treasury).

Estimate of average outstanding Treasury debt during period arising from U.S. loans and repayments under the IMF's General Arrangements to Borrow and Supplementary Financing Facility.

Sum of columns 1 and 2. Transfers to and from the IMF under the U.S. quota subscription or U.S. lending arrangements result in budget outlays and simultaneous receipts of U.S. reserve position in the IMF; these transactions have a zero effect on net outlays and the budget deficit.

Estimate of interest paid or borrowing reduced during period as result of cumulative debt or cash position arising from U.S. transactions with IMF; equals column 3 times average Treasury 3-month bill rate during period. Payments enter the U.S. budget as interest on the public debt; inflows reduce Treasury's need to borrow and thus reduce interest expense.

Enters the U.S. budget as a receipt.

Remuneration on U.S. creditor position; prior to 1975, remuneration was 1.5 percent, although special income distributions were made in 1970 and 1971 which raised the effective rate to 2.0 percent in those years. From 1975, the rate was based on short-term market interest rates in the five largest IMF members (U.S., U.K., Germany, France, Japan). Enters the U.S. budget as a receipt. Payments are made by IMF annually, as of April 30.

Reflects changes in the dollar value of the U.S. reserve position in the IMF due to an appreciation (-) or depreciation (+) of the dollar in terms of the SDR. Enters the U.S. budget as a positive or negative net outlay.

Interest earned on investments of German marks and Japanese yen acquired from U.S. drawing on IMF in November 1978. Enters the U.S. budget as part of the net profit or loss of the Exchange Stabilization Fund of the Treasury, recorded as a positive or negative net outlay.

Equal to the sum of columns 4 through 8.

Remuneration accrued May-December 1982, following receipt of remuneration for IMF fiscal year ending April 1982.

TABLE 2

Estimated Annual Treasury Public Borrowing Requirements and Financing Costs Related to U.S. Transactions Under U.S. Quota and U.S. Loans to IMF, FY 1970-1983I
(millions of dollars)

During U.S. Fiscal Year	Dollar Funds Supplied(-) or Received(+) by Treasury During Period, Arising From: Transactions Under U.S. Quota 1/	U.S. Loans to IMF 2/	Total 3/	Estimated Treasury Borrowing Cost(-) or Reduction(+) Arising from Debt or Cash Position Related to IMF Transactions 4/
1970	-802	-	-802	-66
1971	+908	-	+908	-28
1972	+986	-	+986	+26
1973	-50	-	-50	+42
1974	-471	-	-471	+50
1975	-1,073	-	-1,073	-32
1976	-1,205	-	-1,205	-63
TQ	-702	-	-702	-32
1977	-105	-662	-767	-164
1978	+963	+39	+1,002	-196
1979	+1,333	+633	+1,966	-83
1980	-412	-303	-715	-78
1981	-2,359	-537	-2,896	-376
1982	-1,826	-345	-2,171	-619
1983I	-572	-160	-732	-134
Total Net Change: 7/1/69-12/31/82	-5,387	-1,335	-6,722	-1,753
Annual Average Change:	-399	-99	-498	-130

Footnotes to Table 2

1/ U.S. transfers of dollars to the IMF (i.e., an outflow of dollars from Treasury) and dollar balances received by the U.S. from the IMF and from sales of foreign currency drawn by the U.S. from the IMF (i.e., an inflow of dollars to the Treasury).

2/ U.S. loans and repayments under the IMF's General Arrangements to Borrow and Supplementary Financing Facility; includes interest received in dollars by the U.S.

3/ Total net dollar funds supplied or received by Treasury annually; indicates impact on Treasury public borrowing requirements.

4/ Estimated cost of servicing annual average of outstanding public debt associated with transactions under U.S. quota and on U.S. loans to IMF; from Table 1.

APPENDIX D

MULTILATERAL DEVELOPMENT BANKS
FY 1984 BUDGET REQUEST AND OUTLAY ESTIMATES
(dollars in thousands)

	Budget Authority/ <Program Limitation>	Outlays
International Bank for Reconstruction and Development		
Paid-in Capital	109,721	36,855
Callable Capital	<1,353,220>	
IBRD	1,462,941	36,855
International Development Association		
IDA IV-V	---	416,000
IDA VI	1,095,000	493,000
IDA	1,095,000	909,000
Inter-American Development Bank		
Paid-in Capital	58,001 *	30,321
Callable Capital	<1,230,965>*	
Subtotal	1,288,966	30,321
Fund for Special Operations (FSO V-VI)	41,123	259,868
Fund for Special Operations (FSO VII)	72,000 *	---
Inter-American Investment Corp.	20,000 *	4,000
IDB	1,422,589	294,189
Asian Development Bank		
Paid-in Capital	6,944 *	27,353
Callable Capital	< 224,519>*	
Subtotal	231,463	27,353
Asian Development Fund (ADF II - III)	17,116	82,710
Asian Development Fund (ADF IV)	130,000 *	---
ADB	378,579	110,063
African Development Bank		
Paid-in Capital	17,987	17,987
Callable Capital	< 53,960>	
AFDB	71,947	17,987
African Development Fund		
AFDF I-II	---	37,500
AFDF III-IV	50,000 *	1,000
AFDF	50,000	38,500
TOTAL BUDGET AUTHORITY	1,618,391	
TOTAL PROGRAM LIMITATION	<2,862,663>	
TOTAL OUTLAYS		1,406,594

* Authorization legislation to be sought

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

For Immediate Release
March 4, 1983

Contact: Charlie Powers
566-2041

Treasury Department to Recommend Legislation on Federally Guaranteed Tax-Exempt Bonds

The Treasury Department today announced that it will seek an amendment to the Internal Revenue Code to deny tax-exempt status to certain governmental obligations that are Federally guaranteed.

Present law permits state and local government agencies that issue tax-exempt obligations to invest the proceeds of their bond issues in certificates of deposit of Federally insured financial institutions. These certificates of deposit are pledged as security for repayment of the tax-exempt bonds. The amounts deposited with the financial institutions are then loaned to customers of the financial institutions for projects qualifying for tax-exempt financing.

Recently, it has been determined that these certificates of deposit will be insured by the Federal Savings & Loan Insurance Corporation (FSLIC) or the Federal Deposit Insurance Corporation (FDIC), in an amount up to $100,000 per bondholder. Because the certificates of deposit are pledged to secure repayment of the tax-exempt bonds, the presence of the FSLIC and FDIC insurance effectively provides a Federal guarantee of these bond issues. Providing these effective Federal guarantees violates the established Federal policy against Federal guarantees of tax-exempt obligations. The availability of these Federal guarantees also will increase the volume of tax-exempt bonds that are issued. In addition, the Federal guarantees of these bonds may cause serious distortions in the market for tax-exempt securities, particularly the market for general obligation bonds issued by state and local governments.

Under the Treasury proposal, tax-exempt status will be denied for bonds that are guaranteed directly or indirectly by Federal agencies or instrumentalities which insure deposits made with financial institutions. The proposed change in the law would be effective for bonds and other evidences of indebtedness issued after April 15, 1983. The proposed change would not apply, however, to any obligation issued pursuant to a written commitment that was binding on March 4, 1983, and at all times thereafter.

# # #

R-2068

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
March 7, 1983

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(202) 566-2041

TREASURY ANNOUNCES PUBLIC MEETING TO DISCUSS U.S.-IRELAND TAX TREATY ISSUES, ON APRIL 12, 1983

The Treasury Department today announced that it will hold a public meeting on April 12, 1983, to solicit the views of interested persons regarding issues being considered during negotiations of a new income tax treaty between the United States and Ireland.

The public meeting will be held at the Treasury Department, at 2:00 p.m., in room 4125. Persons interested in attending are requested to give notice in writing by April 5, 1983, of their intention to attend. Notices should be addressed to A. W. Granwell, International Tax Counsel, Department of the Treasury, room 3064, Washington, D.C. 20220.

Today's announcement of the April public meeting follows the conclusion of the first round of negotiations between representatives of the United States and Ireland to develop a new income tax treaty for the avoidance of double taxation and the prevention of tax evasion. The existing treaty between the United States and Ireland was signed in 1949.

The Treasury seeks the views of interested persons in regard to the full range of income tax treaty issues, as well as other matters that may have relevance to an income tax treaty between the United States and Ireland. The April 12, public meeting will provide an opportunity for an exchange of views, and will permit discussion of the United States position in regard to the issues presented.

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R-2069

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE

March 7, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $6,203 million of 13-week bills and for $6,204 million of 26-week bills, both to be issued on March 10, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing June 9, 1983			26-week bills maturing September 8, 1983		
	Price	Discount Rate	Investment Rate 1/	Price	Discount Rate	Investment Rate 1/
High	97.946a/	8.126%	8.43%	95.895	8.120%	8.61%
Low	97.920	8.229%	8.54%	95.860	8.189%	8.69%
Average	97.926	8.205%	8.52%	95.869	8.171%2/	8.67%

a/ Excepting 3 tenders totaling $3,000,000.

Tenders at the low price for the 13-week bills were allotted 62%.
Tenders at the low price for the 26-week bills were allotted 23%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	Received	Accepted
Boston	$ 90,150	$ 40,150	$ 156,790	$ 72,940
New York	12,633,950	4,306,050	12,676,450	4,958,725
Philadelphia	127,055	67,555	82,855	58,605
Cleveland	93,175	73,175	66,725	36,725
Richmond	46,275	40,275	55,900	48,050
Atlanta	55,350	55,350	62,000	47,000
Chicago	1,074,185	567,185	731,405	262,555
St. Louis	76,145	49,145	80,220	57,680
Minneapolis	21,450	21,450	32,480	12,480
Kansas City	49,990	49,990	53,110	50,940
Dallas	23,915	23,915	20,235	20,235
San Francisco	1,199,930	653,930	1,357,120	340,560
Treasury	254,885	254,885	237,540	237,540
TOTALS	$15,746,455	$6,203,055	$15,612,830	$6,204,035
Type				
Competitive	$13,383,195	$3,839,795	$13,205,270	$3,796,475
Noncompetitive	973,560	973,560	738,960	738,960
Subtotal, Public	$14,356,755	$4,813,355	$13,944,230	$4,535,435
Federal Reserve	1,253,500	1,253,500	1,240,000	1,240,000
Foreign Official Institutions	136,200	136,200	428,600	428,600
TOTALS	$15,746,455	$6,203,055	$15,612,830	$6,204,035

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 8.120%.

R-2070

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
March 7, 1983

Contact: Charles Powers
(202) 566-2041

TREASURY DEPARTMENT ANNOUNCES STATUS OF
INCOME TAX TREATY NEGOTIATIONS WITH NETHERLANDS ANTILLES

The Treasury Department announced today that further discussions between the Government of the United States and the Government of the Netherlands Antilles for the purpose of agreeing on a new income tax convention were held in Washington in late February.

During these discussions the two Delegations were able to narrow their differences significantly. As for the issues that remain open, the United States set forth its position, which the Netherlands Antilles Government is now considering. The Netherlands Antilles will communicate the results of this consideration to the Treasury Department shortly.

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R-2071

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-204

For Release: March 8, 1983 Contact: Charles Powers (202) 566-204

Treasury Announces Four Additional Settlements
Between U.S. Banks and Iran

The Treasury Department announced today that it and the Federal Reserve Bank of New York have given the necessary payment clearances and instructions for settlements reached by four United States banks with Iran concerning non-syndicated loan claims against Iran. The four banks are Allied Bank International of New York, First Wisconsin National Bank of Milwaukee, The Fidelity Bank of Philadelphia and American Security Bank of Washington, D.C.

Payment of a total amount of $8,733,000 owing to these banks will be made from the escrow account (known as "Dollar Account No. 2") established at the Bank of England with the deposit of $1.418 billion in January 1981, following the release of the U.S. nationals held hostage in Iran. From the amounts to be paid out of Dollar Account No. 2, three of the four banks will be paying agreed-upon amounts to Markazi in settlement of Iran's claims for interest on blocked Iranian deposits held by those banks.

These settlements closely follow the pattern of the Chemical Bank settlement which was the first settlement reached by a U.S. bank having outstanding loan claims against Dollar Account No. 2. Thus, as of this date, five banks have reached settlements with Iran, and once the four settlements announced today have been implemented, a total of $37.3 million will have been paid out of Dollar Account No. 2. Other U.S. banks are presently meeting with Bank Markazi representatives in London and are in the process of negotiating their respective claims against Iran. Additional bank settlements are expected to follow over the next several months.

John M. Walker, Jr., Assistant Secretary of the Treasury for Enforcement and Operations said, "We are pleased that some of the banks with relatively small claims have been able to negotiate and reach settlements with Iran. We see this as evidence that, as time goes on, the claims settlement process between U.S. banks and Iran will be proceeding expeditiously and routinely."

R-2072

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. March 8, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $12,400 million, to be issued March 17, 1983. This offering will provide $ 925 million of new cash for the Treasury, as the maturing bills are outstanding in the amount of $11,485 million, including $ 763 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities and $2,821 million currently held by Federal Reserve Banks for their own account. The two series offered are as follows:

91-day bills (to maturity date) for approximately $ 6,200 million, representing an additional amount of bills dated June 17, 1982, and to mature June 16, 1983 (CUSIP No. 912794 CD 4), currently outstanding in the amount of $11,601 million, the additional and original bills to be freely interchangeable.

182-day bills for approximately $ 6,200 million, to be dated March 17, 1983, and to mature September 15, 1983 (CUSIP No. 912794 DQ 4).

Both series of bills will be issued for cash and in exchange for Treasury bills maturing March 17, 1983. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

R-2073

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, March 14, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on March 17, 1983, in cash or other immediately-available funds or in Treasury bills maturing March 17, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

TREAS.

FOR RELEASE UPON DELIVERY
EXPECTED AT 10:00 A.M.
Wednesday, March 9, 1983

STATEMENT OF THE HONORABLE
DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE THE SUBCOMMITTEE ON FOREIGN OPERATIONS
COMMITTEE ON APPROPRIATIONS
UNITED STATES SENATE
MARCH 9, 1983

Mr. Chairman, I am pleased to have this opportunity to appear before you today to explain the Administration's funding request for the multilateral development banks and to ask for your prompt and favorable consideration of this request.

We are all well aware of the fact that the international financial and economic system is experiencing very serious strains. The difficulties we face are without precedent in the postwar era and pose a very serious threat to the efforts being made, both domestically and internationally, to restore growth and vitality to the world economy.

I understand that the Appropriations Committee will be considering separately legislation providing for U.S. participation in an increase in IMF resources. The IMF is the centerpiece of a comprehensive strategy to deal with current strains in the international financial system in the orderly manner essential for U.S. and global economic recovery. The IMF must have adequate resources to fulfill its vital responsibilities for promoting sound economic adjustment and I urge your prompt approval of this vital legislation.

Global conditions pose particularly severe problems for the countries of the developing world. The United States has a long tradition of cooperating with developing countries, through both bilateral and multilateral channels, to assist them in accelerating the development process. We have done so both for altruistic reasons, and in pursuit of our own interests. If the developing countries, especially the poorest ones, are to continue to have an opportunity to participate fully in international growth, it is clear that immense challenges will have to be met during the remainder of this decade.

The most important contribution the United States can make to world development is to pursue sound economic policies at home. A vigorous U.S. economy firmly set on a path of sustained and non-inflationary economic growth will be of immeasurable help to the global economy. We have set out a comprehensive course to domestic economic recovery and will continue to work closely with the Congress to assure it is followed.

At the same time we must recognize that global economic conditions have a direct impact on the health of the U.S. economy, and that the international economic environment can be an important force for either enhancing or thwarting our domestic recovery efforts. It is thus in our own economic self-interest to encourage sound and sustainable growth in the developing world. A prospering and economically stable developing world also serves important U.S. political, strategic, and humanitarian interests.

It is the view of the Administration that the multilateral development banks do contribute effectively to economic growth and development and that active U.S. support for these institutions is critical to our security and economic interests. Those interests include:

<u>National Security Interests</u>

At a time when global economic difficulties are exposing nearly all of the poorer developing countries to serious threats of political, economic, and social instability, the MDBs are capable of providing a valuable contribution to our national security and other foreign policy objectives in each of the major regions of the world and in countries of particular interest to us. One need only scan the list of the largest MDB borrowers -- Mexico, Brazil, Argentina, Indonesia, Korea, Pakistan, Thailand, the Philippines, Turkey, and Egypt -- to recognize that the MDBs are lending to countries of great importance to us. The IDB is especially important for our relations with Latin America and the Caribbean. The MDBs are not providing any assistance to such hostile nations as Vietnam, Cuba, Iran, Afghanistan, and Cambodia.

There is also the growing importance of our dependence on critical raw materials from the developing world. The United States, for example, depends upon the developing countries for all of its tin imports, 90 percent of its bauxite, and 76 percent of its cobalt. The MDBs have made loans to key producing countries such as Bolivia, Zambia, Zaire, and Indonesia. We and the rest of the world have a vital stake in ensuring the stability of LDC economies which produce critical raw materials and in safeguarding access to these supplies.

The Health of the International Economic System

In U.S. FY 1982, MDB loan commitments totalled $16.8 billion. This made the MDBs by far the largest official source of external capital for the developing world. As such, they can contribute in a major way to economic growth and stability in developing countries, and to the expansion of trade between the developing and the industralized nations. By improving their policy advice, preparing development projects based upon sound economic criteria, and insisting upon rational economic policies within recipient countries, the MDBs can continue to be an important respected force in the international economy -- one which promotes the open, competitive, market-oriented economic system.

The United States continues to urge these institutions to strengthen their role in advocating an open trading system, realistic foreign exchange rates, the use of markets to help determine resource allocations, sound pricing policies, cost recovery in investment projects, reliance upon the private sector, and sensible fiscal and monetary policies. With such efforts the impact of the MDBs can result in a significant contribution to the health of the world economy.

Direct U.S. Economic Benefits

There are direct benefits to the United States in increased exports to developing countries which borrow from the MDBs. Generally, non-OPEC developing countries account for over 25 percent of U.S. manufactured exports. In a time of high unemployment, these markets are even more important for American workers.

In addition, the relatively limited U.S. paid-in subscriptions and contributions to the soft windows can result in larger expenditures on U.S. goods and services. Currently, procurement of American goods and services for projects assisted by the MDBs is running at approximately 1.2 billion dollars per year, benefitting virtually all regions of the United States. At the same time U.S. budgetary outlays for U.S. paid-in subscriptions and contributions to the soft windows have been approximately $1.0 billion per year. Thus, there is a net positive return on U.S. contributions just in terms of procurement, and we are working to improve on that record.

In terms of description of goods sold, the major categories were mechanical equipment, consultant services, chemicals, electrical equipment, school equipment, medical equipment and supplies.

We are working to improve the effectiveness of the MDBs so as to maximize their contribution to overall economic growth in the developing countries and United States interests. At the same time, we are conscious of budgetary concerns, and are trying to ensure that the MDBs make the most efficient use of their resources and that our interests are advanced at the lowest possible costs. By improving their efforts in such areas as project preparation, economic analysis and technical assistance, the MDBs can fulfill a unique role in promoting the sound economic policies and market-oriented institutions necessary to better integrate the developing countries into the international economic system.

THE APPROPRIATION REQUEST

The Administration's request for fiscal year 1984 calls for $1,618.4 million in budget authority and $2,862.7 million in callable capital under program limitations for subscriptions and contributions to the multilateral development banks.

We believe funding at this level is essential to meet our existing international commitments from previous replenishments and also to meet the funding requirements for new replenishments in the regional development banks, which this Administration has negotiated.

For more than a year, the Administration has been engaged in negotiations to replenish the hard and soft loan windows of the Inter-American and the Asian Development Banks. Throughout these negotiations we have carefully considered the views expressed by the Congress and have tried to achieve the major recommendations of our Assessment. The new replenishments represent important further steps toward implementing those recommendations.

Specifically, the new replenishments are consistent with the Assessment's recommendations to reduce overall contributions to the soft loan windows and the proportion of capital subscriptions paid-in while still providing assistance to the poorest developing countries.

While the substantial reduction in funding for the soft windows will limit concessional lending programs, we have managed carefully to concentrate funding on the poorest regions and countries. The replenishment for the IDB's Fund for Special Operations will be about $1 billion less than the previous replenishment, but Latin America has the highest per capita GNP of the developing regions of the world. By contrast, the replenishments for the Asian Development Fund and African Development Fund will be about $1 billion and $200 million larger respectively.

We are also urging that the MDBs use their resources more effectively, so that the poorest countries receive the benefits of these programs. We have been working with the Banks to ensure: (1) greater selectivity and policy conditionality within projects and sector programs; (2) more emphasis on catalyzing private sector flows; and (3) firm implementation of graduation from hard loan windows and maturation from soft windows. Effective use of these policies should permit lower funding levels and at the same time ensure that scarce resources are concentrated on those countries which can best employ them and which are in the greatest need.

The Assessment of U.S. participation in the MDBs recommended that the U.S. phase-down and eventually phase-out paid-in capital in future MDB replenishments. The proposed levels in the new replenishments represent a declining reliance on paid-in capital as the institutions have matured financially. It is a balanced compromise that reflects our budgetary situation and the views of both the Congress and the capital markets.

In the case of the IDB, the new level of 4.5 percent paid-in will result in annual budgetary savings of almost $40 million per year, or $160 million over the four-year period of the replenishment, compared with the 7.5 percent paid-in level of the last replenishment. The reduced level of paid-in was accompanied by an increase in the convertible currency subscriptions of the borrowing member countries. The borrowing member countries will now provide 100 percent of their paid-in capital in convertible currencies as compared to 66 percent in the last replenishment.

With regard to the Asian Development Bank, ADB management initially proposed maintaining the ten percent existing level of paid-in for the upcoming General Capital Increase (GCI). While discussions about the size and financing of the GCI are still ongoing, we expect the level of paid-in capital eventually agreed upon will be approximately 5 percent.

By reducing the proportion of paid-in capital, we reduce the budgetary cost to U.S. taxpayers while maintaining the financial soundness of these institutions.

International Development Association (IDA) Supplemental

In addition to the fiscal year 1984 request, the stretch out of our contributions to IDA VI necessitates a $245 million fiscal year 1983 supplemental request.

The United States was expected to provide $1.08 billion annually for three years to IDA under the original internationally negotiated funding arrangement. However U.S. contributions have been far short of this expectation because our contributions were subsequently stretched over four years. We provided only $500 million in FY 1981 and $700 million a year in fiscal years 1982 and 1983. Other donors took up much of the slack by agreeing to release their second and third installments to IDA, and to provide an additional $2 billion to sustain the lending in FY 1984.

The $245 million in the FY 1983 supplemental is a critical component in the President's foreign assistance program. The United States needs to meet the existing schedule of contributions in order to demonstrate both our ability to live up to international funding commitments and our desire to work constructively with other members to enhance the impact of IDA's operations.

IDA is a significant element of economic cooperation with our allies and is the largest single source of concessional assistance. With underdeveloped resource bases, small productive capacities, and low per capita incomes, most IDA recipients have very limited access to external resources from private sources, and they have also been hardest hit by the global recession. Consequently IDA operations are very important to these countries, many of which -- such as Kenya, Sri Lanka, Pakistan and Sudan --- are of strategic and economic importance to the United States. IDA operations are also important to U.S. humanitarian interests in that more than 80 percent of IDA's commitments have been to countries that in 1980 had per capita incomes of $410 or less. In addition, at our urging, IDA has begun to focus on the difficult development problems of Sub-Saharan Africa.

Full funding of the Administration's request for IDA is necessary to avoid further disruptions in IDA's lending operations. It is also important to demonstrate the U.S. long-standing commitment to work constructively with our allies to assure that the poorest countries are provided an opportunity to participate in the process of growth and development.

BUDGETARY IMPLICATIONS

The FY 1984 request for the MDBs represents an increase of $326.4 million in budget authority, and $502 million under program limitations over the FY 1983 appropriation. (This does not include the FY 1983 supplemental request of $245 million for IDA). The bulk of the increase ($395 million in budget authority) over last year's appropriation comes as a result of meeting the shortfall in our commitments to IDA VI.

THE WORLD BANK GROUP

-- For the International Bank for Reconstruction and Development (IBRD), we propose $109.7 million in budget authority and $1,353.2 million in callable capital under program limitations for the third of six installments of the U.S. share of the 1981 General Capital Increase.

-- For the International Development Association, the Administration is requesting $1,095 million in fiscal year 1984, which together with the $245 million being requested in the supplemental appropriation for fiscal year 1983 will complete the U.S. contribution to IDA VI.

THE INTER-AMERICAN DEVELOPMENT BANK (IDB)

-- For subscription to IDB capital, the Administration is submitting and seeking Congressional approval of authorization legislation for an increase in the U.S. subscription to the capital of the Bank. Included in the FY 1984 appropriation request is the first of four equal annual subscriptions consisting of $58 million in budget authority for paid-in capital and $1,231 million under program limitations for callable capital.

-- For the Fund for Special Operations (FSO), the Administration is submitting and seeking Congressional approval of authorization legislation for a $290 million U.S. contribution to the FSO. The first tranche of $72.5 million is being sought in the FY 1984 appropriation request. Together with prior unfunded requests amounting to $41.1 million, the total FY 1984 request for the FSO is $113.6 million.

-- Partially modeled after the International Finance Corporation, the Inter-American Investment Corporation would be a separate entity which provides development assistance to the private sector in Latin America and Caribbean. The member countries of the Inter-American Development Bank have discussed formation of such a Corporation for a number of years and a meeting was recently held to seek an agreement on the capitalization of the IIC. After the agreement is completed, the Administration will seek authorization from the Congress. The $20 million requested for FY 1984 is what we envision to be the initial U.S. subscription.

THE ASIAN DEVELOPMENT BANK

-- For the Asian Development Bank (ADB), the FY 1984 request will depend ultimately on the size of the third general capital increase now being negotiated. We will submit and seek authorization legislation for this replenishment as soon as the negotiations are completed. The FY 1984 request for the ADB reflects the earlier negotiation position of the United States. We now expect that our share of the new replenishment will result in slightly larger numbers than what currently appears in the Budget. Consequently, we will submit a budget amendment when negotiations are completed. The current ADB management proposal calls for a U.S. paid-in capital subscription of $66.2 million and $1,257 for callable capital over five years. The proposal implies a likely request level of $13.2 million for budget authority and $251.4 million under program limitations -- a modest increase over the levels in the January budget estimates, ($6.9 million paid-in and $224.6 million under program limitations). The amount of paid-in capital represents a significant reduction from the $20.4 million annual amount in the last general capital increase.

-- For the Asian Development Fund (ADF), we are requesting $147 million which includes $130 million for the first tranche of the third replenishment (ADF IV), $3 million for the remaining proportion of our share of the second replenishment (ADF III), and $14 million for an unfunded portion of the first replenishment (ADF II). We are submitting and seeking Congressional approval of authorizing legislation for an increase in U.S. contributions to the ADF.

THE AFRICAN DEVELOPMENT BANK

-- U.S. membership in the African Development Bank (AFDB) was authorized in 1981 as was a U.S. subscription of $359.7 million of AFDB capital. The Congress appropriated the first installment of the U.S. subscription to the AFDB in 1981. This installment included $17.99 million for subscription to paid-in capital and $53.96 million, under program limitation authority, for subscription to AFDB callable capital. A second installment with identical amounts for paid-in and callable capital subscriptions is being sought in FY 1984.

-- In 1982, negotiations for a third replenishment of African Development Fund (AFDF III) resources were completed. Legislation authorizing a $150 million increase in U.S. contributions to this replenishment was submitted to, but was not enacted by the 97th Congress. This legislation has been resubmitted to the 98th Congress. Upon enactment of this legislation the United States will provide its first $50 million installment under authority of the 1983 Continuing Resolution. The FY 1984 request is for $50 million for the second installment to AFDF III.

CONCLUSION

In conclusion, MDB lending for economically sound projects is an important element of the international community's efforts to spur sustainable economic growth and greater stability in the developing world. Such growth is an important element in the health of the world economy, and also has considerable impact on the U.S. economy.

Continued emphasis on the MDBs to channel a substantial proportion of U.S. development assistance is also fully consistent with the need to ensure cost-effectiveness and to avoid unnecessary budget outlays.

Attractive features of the MDBs include cost sharing and the leveraging of U.S. contributions through MDB borrowing in world capital markets.

We strongly urge your support for this program. It represents the minimum amount of financial support required to safeguard the U.S. leadership role in these institutions.

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. March 9, 1983

TREASURY TO AUCTION $7,750 MILLION OF 2-YEAR NOTES

The Department of the Treasury will auction $7,750 million of 2-year notes to refund $4,695 million of 2-year notes maturing March 31, 1983, and to raise $3,055 million new cash. The $4,695 million of maturing 2-year notes are those held by the public, including $1,202 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities.

The $7,750 million is being offered to the public, and any amounts tendered by Federal Reserve Banks as agents for foreign and international monetary authorities (including the $1,202 million of maturing securities) will be added to that amount.

In addition to the public holdings, Government accounts and Federal Reserve Banks, for their own accounts, hold $888 million of the maturing securities that may be refunded by issuing additional amounts of the new notes at the average price of accepted competitive tenders.

Details about the new security are given in the attached highlights of the offering and in the official offering circular.

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Attachment

R-2075

HIGHLIGHTS OF TREASURY
OFFERING TO THE PUBLIC
OF 2-YEAR NOTES
TO BE ISSUED MARCH 31, 1983

March 9, 1983

Amount Offered:

To the public	$7,750 million

Description of Security:

Term and type of security	2-year notes
Series and CUSIP designation	Series S-1985 (CUSIP No. 912827 PG 1)
Maturity date	March 31, 1985
Call date	No provision
Interest rate	To be determined based on the average of accepted bids
Investment yield	To be determined at auction
Premium or discount	To be determined after auction
Interest payment dates	September 30 and March 31
Minimum denomination available	$5,000

Terms of Sale:

Method of sale	Yield Auction
Competitive tenders	Must be expressed as an annual yield, with two decimals, e.g., 7.10%
Noncompetitive tenders	Accepted in full at the average price up to $1,000,000
Accrued interest payable by investor	None
Payment by non-institutional investors	Full payment to be submitted with tender
Deposit guarantee by designated institutions	Acceptable

Key Dates:

Deadline for receipt of tenders	Wednesday, March 16, 1983, by 1:30 p.m., EST
Settlement date (final payment due from institutions)	
a) cash or Federal funds	Thursday, March 31, 1983
b) readily collectible check	Tuesday, March 29, 1983

TREASURY NEWS
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STATEMENT OF THE HONORABLE JOHN M. WALKER, JR.
ASSISTANT SECRETARY OF THE TREASURY
FOR ENFORCEMENT AND OPERATIONS
BEFORE THE
SUBCOMMITTEE ON GOVERNMENT INFORMATION, JUSTICE
AND AGRICULTURE
HOUSE COMMITTEE ON GOVERNMENT OPERATIONS
MIAMI, FLORIDA
FEBRUARY 26, 1983

Treasury's Drug Interdiction Program After South Florida

Mr. Chairman, Senators, Members of the Committee, thank you for this opportunity to appear before you today on the subjects of Federal drug enforcement and Posse Comitatus implementation. With me today is Commissioner von Raab, who will be testifying on the specific interdiction efforts that the Customs Service is now conducting and on new initiatives for enhancement of Customs' drug interdiction program. In my testimony today, I will comment on our overall drug interdiction strategy and how the progress in South Florida relates to our overall enforcement effort.

First, I want to express my sincere appreciation for the continuing interest and support that you have demonstrated in Treasury's and this Administration's efforts to stem the flow of drugs into this country. From the standpoint of Treasury law enforcement, the battle against drug smuggling is our paramount concern. As you are well aware, the costs imposed on our society by drug smuggling, drug use, and the crimes they foster are alarmingly and unacceptably high. Your continued interest and efforts have been a valuable contribution to our overall drug enforcement program. I want to also acknowledge the ongoing support of Treasury law enforcement by the Chairman of Treasury's House Appropriations Subcommittee, Chairman Roybal.

I also want to take this opportunity to commend Senator Paula Hawkins for her tireless efforts in the Senate and as Chairman of the Senate Drug Caucus in the war against drug abuse and drug trafficking. We are constantly reminded by her encouragement and real support that drug law enforcement has a working partner on Capitol Hill.

The U.S. Government's efforts to reduce the supply of illegal drugs have four basic lines of defense. First, through crop eradication and substitution efforts coordinated with the governments of drug-producing countries, raw materials for drug production can be prevented from being produced or destroyed while they are still in the ground. Second are the enforcement measures abroad to stop the commerce in drugs that are still in transit: from the harvest of these raw materials to the point from which the drugs will be smuggled across our borders. The third line of defense, drug interdiction, is our final line of defense against drugs entering the country if the eradication and foreign enforcement efforts fail. It is the last opportunity that the government has to keep drugs from entering U.S. distribution networks and, significantly, it is also the last opportunity to intercept drug supplies while they are still in their bulk, undiluted form. The fourth line of defense consists of drug and financial investigations that target the major drug trafficking organizations in the United States. The purposes of these investigations are to seize drugs, to prosecute and convict major offenders for drug violations, to target the major trafficking organizations and their money launderers for financial crimes such as Bank Secrecy Act (Title 31) and income tax violations (Title 26), and to seize and forfeit assets wherever possible. These investigations often lead to information that results in drug interdictions.

Each of these four phases of drug enforcement must receive our full attention and support. A concentration on any one at the expense of another would result in a weakening of our total enforcement effort. All are equally important. Interdiction at the border remains a critical part of the overall drug enforcement process. It is at the border that drugs enter this country in their purest form and largest quantity. The criminal stature of the individual who actually smuggles drugs into the U.S. ranges from the high-level, sophisticated smuggler with organized crime connections to the low-level "mule" commissioned specifically to serve as a courier. Whether this individual is a high-level smuggler or a low-level "mule", he or she will still have intelligence that can be developed by an investigation aimed at both the foreign source of the drugs and at their destination in this country. Hence, the smuggler provides an indispensable link between the foreign origin of the drugs and the points of domestic delivery. Historically, some of the biggest international conspiracy cases in drug enforcement have been initiated by the capture or detection of couriers who, either unwittingly or in a cooperative manner, led investigators to top violators. The fact that most individuals arrested in interdiction cases are typically low-level violators cannot justify a failure to follow up and investigate these arrests. Even the low-level smuggler knows where and from whom he got the drugs and knows where and to whom he is to deliver them. For Customs purposes, the low-level smuggler has information that can lead to important seizures and arrests. Thus, we can see that border interdiction is critical, but still, if it is to have long-term effectiveness, it must be conducted in conjunction with the other phases of drug supply reduction.

When I last appeared before this Committee, in August of last year, I reported that our drug interdiction program in South Florida had been considerably strengthened by the support and technical assistance provided by the Defense Department. At that time, we had seen the positive results of increased radar surveillance, both airborne and stationary, and the use of Cobra helicopters for pursuit and seizure of smuggler aircraft. This enhancement of our detection, pursuit and apprehension capabilities produced measurable results in South Florida, such as in the reduction in the air smuggling traffic in the Florida area and the lowering of the crime rate in greater Miami. We also began to note changes in the locations and methods of the drug smuggler. Air drops near the Bahamas, diversions of air smuggling up the Atlantic coast and into the Gulf States, and an increase in smuggling through concealment by commercial air passengers all provided indications that our Florida operations were causing the smugglers to change their method of operation and to divert to other areas. It was apparent that we were disrupting their operations and forcing them to incur increased expense and risk of apprehension.

These developments pointed to the need for a Federal response that was nationwide in scope. I believe that we would be remiss as an Administration if we did not attempt to correct a situation wherein we know that numerous private aircraft are bringing large quantities of drugs into the country. The strategy and capability which we hope to develop will be, I believe, cost-effective in terms of utilizing equipment already in the hands of the Department of Defense, at a cost which will not exceed resources already requested in the Customs 1984 budget. Again I want to state that the assistance which you and Senator DeConcini and members of your respective staffs have given to the Treasury Department and continue to give in this matter is very helpful and represents a bipartisan effort against the national problem which threatens the well-being of our country.

Even before the inception of the South Florida Task Force, we recognized that the threat posed by smuggling of contraband in small aircraft was of severe proportions, particularly in the Florida area. Understandably, Customs chose to concentrate its air interdiction resources in this strategic area of the country. Customs' ongoing air operations became more critical when the South Florida Task Force became operational in March of 1982.

As our South Florida operations progressed, it became increasingly clear, from diversions of air smuggling traffic, that Customs' air interdiction capability needed to be expanded to a national basis. The problem was clarified in the 1983 National Air Threat Study, which Customs submitted to Congress in mid-November of 1982. Accompanying this document was a revised National Air Program Strategy, which was based on an earlier strategy but was updated to reflect the DOD contributions that had been authorized under the Posse Comitatus legislation. Treasury has continued to refine this strategy and work toward its implementation. Through consultations with the Defense Department and this Committee and its staff, we have been better able to identify the particular components of an expanded program.

As you know, Treasury strongly supports the establishment of an air interdiction capability for Customs that will provide for our three critical air interdiction needs: One - detection of intruding aircraft, Two - interception and tracking of the aircraft following detection, and finally, Three - apprehension of air smuggler suspects followed by arrests and seizures. The magnitude of the drug smuggling threat, and the increasing sophistication in the methods of the drug smuggler, dictate that the equipment for this undertaking be of a highly advanced design. Because of the associated high costs of acquisition, operation, and maintenance, we are looking to the Department of Defense for the loan of the necessary aircraft and radar systems.

On January 17 of this year, our efforts culminated in my formal request to the Defense Department for general categories of aircraft and detection equipment, with suggestions for specific hardware that would provide the capability to accomplish all three phases of air interdiction on a national basis. Since that time, the Defense Department, assisted by your able Committee staff and Customs, has been researching their inventory, and I believe they are now close to making final recommendations based in great part upon suggestions you have made. The Department of Defense and particularly, Jim Juliana, have been tremendously cooperative to date, and I have every expectation that their continued cooperation will result in the appropriate equipment being provided.

Since I last appeared before you, this Administration has developed a national drug investigative strategy involving the 12 drug task forces announced by the President last October. These task forces will coordinate efforts of enforcement bureaus of Treasury and Justice in conducting investigations against the major drug trafficking organizations in this country. Three Treasury Bureaus will be active in these task forces: IRS and Customs, which will target the financial aspects of the trade, and ATF, which will concentrate on firearms trafficking by drug dealers.

Customs and IRS will jointly conduct financial investigations against major drug trafficking organizations and their money launderers. Our financial investigative techniques will concentrate on disrupting the illegal laundering of drug profits by asset forfeitures, the imposition of penalties and jeopardy tax terminations and assessments. Customs and IRS agents will seek prosecutions of drug-related violations of the Bank Secrecy Act and the income tax laws.

ATF agents will target major drug traffickers who violate the firearms and explosives laws. They will also concentrate on the insidious traffic in machine guns and silencers in support of the drug trade. Their attention will also be focused on violations of the firearms laws committed by members of outlaw motorcycle gangs who are trafficking in drugs.

The ultimate goal of Treasury Department efforts in this program will be to destroy as many high level drug trafficking organizations as possible, both by putting them in jail and by seizing their assets.

I would like to briefly comment on our South Florida enforcement effort, past and future, and how the lessons learned will be carried forward to the rest of the country.

With regard to our effort in South Florida, I am pleased to report to this Committee that the Departments of Justice and Treasury have reached agreement on the organization and structure for the Permanent Florida Joint Task Group to conduct interdiction-related investigations. The basic principle which has supported the successful Task Group operation in the past will be retained. Just as before, DEA and Customs will jointly conduct drug smuggling investigations, and each agency will remain responsible for management of its personnel and resources. This group can serve as a model for similar groups outside of Florida.

In addition to DEA and Customs, the Bureau of Alcohol, Tobacco and Firearms has played an increasingly significant role in Florida in the battle against drug smuggling organizations and violent crime through its investigations of drug-related weapons violations. In the 7 months since being deployed in South Florida ATF agents have opened 385 investigations, leading to 112 arrests, 90 indictments, and 49 convictions. They have seized 810 weapons, 319 of which are Title II weapons, associated with gangland operations. If our struggle against drug smuggling is to succeed, we believe it is critical that we continue to attack the important connection between drug smuggling organizations and illegal trafficking in firearms, both here in Florida and across the country.

I am sorry to report to this Committee that on December 2, ATF lost Special Agent Ariel Rios during an undercover firearms investigation in Miami. Special Agent Alexander D'Atri was seriously wounded in the same incident. Events such as this one remind us, once again, that the drug trafficker is a vicious and ruthless enemy.

With respect to financial investigations, the highly successful Operation Greenback, jointly spearheaded by the IRS and Customs in Florida, will continue to attack the asset base of drug traffickers and money launderers. In just the past year, money laundering operations responsible for the processing of approximately 400 million drug dollars per annum have been destroyed. Indeed it is Greenback's success here in Florida that has led to the establishment of 20 additional financial task forces across the country and to the heavy financial investigative emphasis in the 12 new task forces announced by the President in the fall.

I would like to close with some general observations about the importance of our task. We are now at a critical juncture in the war against drug smugglers. The South Florida Task Force, under the leadership of Vice President Bush and the day-to-day guidance of his able Chief of Staff, Admiral Murphy, has broken new ground in linking interdiction and investigation, and in achieving a high degree of cooperation among Federal agencies and with State and local law enforcement. It has demonstrated the value of a concerted Federal enforcement effort that combines drug investigations, interdiction, financial investigations, DOD support, and enforcement against firearms trafficking. However, we have to recognize that the drug smuggling and drug trafficking problem is of enormous dimensions. It had flourished amid conventional law enforcement efforts for many years. It is our view that the additional investigative component represented by the new Task Forces, and the enhanced air interdiction capability represented by the planning that we, with the aid of this Committee, have undertaken, will be essential to the overall Federal drug enforcement effort, if we are to have a permanent effect on drug trafficking and the enormous volume of related crime that it supports.

Finally, as we undergo nationwide expansion of the drug enforcement effort, we must heed the central lesson of South Florida - full and complete interagency cooperation. As cooperation has been the linchpin of our program here in Florida, it will be the linchpin of our strategy nationwide.

I appreciate the opportunity to appear before you to review our progress and discuss any pertinent issues. I would be pleased to provide any additional information the Committee requires, and I welcome any questions you may have.

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FOR IMMEDIATE RELEASE
Wednesday, March 9, 1983

Contact: Charley Powers
566-2041

ADMINISTRATION UNVEILS TAX ALTERNATIVE TO
DOMESTIC INTERNATIONAL SALES CORPORATION (DISC)

Secretary Donald T. Regan and U.S. Trade Representative Bill Brock today announced that the Administration has developed the general elements of a tax alternative to the Domestic International Sales Corporation (DISC), designed to resolve a long-standing GATT (General Agreement on Tariffs and Trade) controversy over the consistency of DISC with U.S. obligations under the General Agreement.

A DISC is a special corporation, added to the Tax Code by the Revenue Act of 1971, designed to defer the tax on export income for the purpose of facilitating the promotion and marketing of U.S. products abroad.

Ambassador Brock, the President's chief adviser on international trade matters, said the Administration's alternative is fully consistent with U.S. obligations under GATT. He emphasized, however, that the alternative will not increase the tax burden on U.S. exporters. In fact, the proposal simplifies many of the complex rules under DISC. In addition, since the proposed alternative conforms to U.S. obligations under GATT, U.S. exporters will be protected against possible retaliation that might otherwise be taken by importers of U.S. products.

Ambassador Brock said that the proposal also complies with GATT rules regarding taxation of export income, under which a territorial tax system -- which exempts from taxation income earned overseas -- is permissible.

Under the GATT, a country does not convey an illegal export subsidy if it exempts from tax income which is attributable to economic activity occurring outside its territory and requires arm's-length pricing in transactions between related parties.

Ambassador Brock explained that, to conform with this GATT standard, the proposal replaces the DISC with a foreign corporation through which export sales would be made. The income from such export sales would be allocated between the foreign sales corporation and a related U.S. company using arm's-length pricing principles from the Internal Revenue Code, or using one of two allocation rules designed for administrative convenience to approximate arm's-length pricing. A portion of the income of the foreign corporation would be exempt from U.S. tax.

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Ambassador Brock said he will continue consultations with the private sector and Members of Congress in an effort to further refine the proposal. He also invited comments by all interested parties.

The proposal must now be recast in the form of legislation for consideration by Congress.

Principal elements of the Administration's proposal are discussed in the attachment.

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ADMINISTRATION PROPOSAL FOR A DISC REPLACEMENT

Introduction

On March 2, 1983, the Cabinet Council on Commerce and Trade approved a proposal for a tax alternative to the Domestic International Sales Corporation (DISC). This proposal meets the U. S. commitment made on October 1, 1982, before the Council of the General Agreement on Tariffs and Trade (GATT) to send a proposal for replacing the DISC to the 98th Congress. This commitment was made to resolve a long-standing GATT controversy over the consistency of DISC with U.S. obligations under Article XVI:4 of the General Agreement. This provision of the Agreement encompasses an obligation not to use export subsidies in certain circumstances.

The Administration's proposal was formulated with four key objectives in mind: 1) consistency with our international obligations under the GATT; 2) avoid any tax increase for exporters; 3) maintenance of revenue neutrality; and 4) preservation of the ability of small businesses to use the tax alternative. The proposal meets all four objectives. In addition, the proposal envisions a substantially simpler procedure for the taxation of exporters than is currently the case under DISC.

The proposal complies with the GATT rules regarding taxation of export income. Under these rules, a territorial tax system -- which exempts from taxation income earned overseas -- is permissible. Accordingly, the GATT does not require that a country tax directly the income from economic activities outside its borders. This is consistent with other GATT provisions which do not prohibit the adoption of measures to avoid the double taxation of foreign source income. The GATT does, however, require that territorial systems use arm's-length pricing rules to allocate income between related domestic and foreign economic entities. Finally, the GATT permits the deferral of direct taxes on export income if an appropriate rate of interest is charged on the deferred sums.

Summary of Proposal

Under the GATT, the United States would not convey an illegal export subsidy if it exempts from tax income which is attributable to economic activity occurring outside the United States and requires an arm's-length pricing in transactions between related parties. To conform with this GATT standard, the proposal replaces the DISC with a foreign corporation through which export sales would be made. The income from such export sales would be allocated between the foreign sales corporation and a related U.S. company using the arm's length procedures prescribed under Section 482 of the Internal Revenue Code (hereafter referred to as the Code), or using one of two allocation rules designed for administrative convenience to approximate arm's-length pricing. The administrative allocation allowed with respect to export sales would be equal to the greater of:

a. 17 percent of the combined taxable income earned by the foreign corporation and its related U.S. manufacturer; or

b. 1.35 percent of the foreign corporation's gross sales, up to 34 percent of the combined taxable income.

Up to the limits described below, the income allocated to the foreign corporpation would be distributed to the parent on a tax free basis. To qualify for this tax treatment, the foreign corporation would be required to undertake certain economic activities outside the United States. Provisions are also included in the proposal to accommodate the special characteristics of small business.

Principle Elements of Proposal

I. U.S. TAXATION OF INCOME EARNED BY THE FOREIGN EXPORT SALES CORPORATION

A foreign export sales corporation will be entitled to an exemption from U.S. tax on a certain portion of its income from export sales (hereafter referred to as Foreign Trading Company Income or FTI) if it conducts economic activities outside the United States. The foreign export sales corporation must be incorporated outside U.S. territory. This requirement reflects the GATT rule that countries need not tax export income from economic processes occurring outside their territorial limits.

II. FOREIGN TRADING COMPANY INCOME

FTI is defined as income (including both profits and commissions) derived in connection with foreign trading gross receipts. Foreign trading gross receipts are gross receipts from:

a. the sale, exchange, or other disposition of export property;

b. the lease or rental of export property which is used by the lessee outside the United States;

c. the performance of services which are related and subsidiary to the sale, exchange, lease, rental, or other disposition of export property by the foreign corporation;

d. the performance of engineering or architectural services for construction projects located outside the United States; and

e. the performance of managerial services in furtherance of the production of foreign export trading gross receipts.

"Export property" generally means property manufactured, produced, grown, or extracted in the United States for direct use, consumption, or disposition outside the United States.

III. ARM'S-LENGTH PRICING RULES

The price at which export property is transferred from the U.S. manufacturer to the foreign sales corporation will be determined using arm's-length transfer pricing principles. As a matter of administrative convenience, this arm's-length requirement will be met by an allocation equal to the greater of:

a. 17 percent of the combined taxable income earned by the U.S. manufacturer and foreign sales corporation; or

b. 1.35 percent of the foreign corporation's gross sales, but not to exceed 34 percent of combined taxable income.

To use either of these administrative allocation rules, the foreign corporation must perform, or have performed on its behalf, the activities described below. As an alternative to the administrative allocation rule, taxpayers may determine the allocation of income by transferring export property to the foreign corporation at a transfer price determined under Section 482 of the Code.

IV. REQUIRED FOREIGN ECONOMIC ACTIVITIES

To be eligible for tax exempt treatment under this proposal, the foreign corporation must:

1. maintain an office outside the United States;

2. maintain books and records in that foreign office;[1]

3. have at least one resident director in the foreign office; and

4. hold an agency agreement or distribution license with respect to the product.

In addition, some or all of the following functions must be performed in part or in total outside the United States by the foreign corporation, or for it on a contract basis, in connection with foreign trading gross receipts.

5. soliciting orders from and negotiating contracts with customers;

6. processing customer orders; and/or

7. billing customers and receiving payments.

If, however, U.S. exporters as part of their normal business practice perform other significant activities outside the United

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1. For purposes of U.S. tax administration and enforcement, it will be necessary for the books and records to be available for examination in the United States.

States, consideration will be given to substituting those for some or all of the functions listed in items 5 through 7. 2/

As long as these foreign presence requirements are met, the foreign corporation will not be subject to U.S. tax on a portion of its FTI. These foreign presence requirements are necessary to conform to the GATT rule which allows for the exemption from taxation of income related to the economic processes occurring outside the exporting country. It should be noted, however, that these foreign presence requirements do not prevent a foreign corporation from maintaining an office in the United States, or from concluding contracts to have activities performed on its behalf in the United States.

V. DEFINITION OF U.S. TERRITORY

For the purposes of this proposal, the U.S. territories of Guam, the Virgin Islands, and the Northern Mariana Islands will be considered outside the territory of the United States. This definition conforms to the definition of territory as customs territory used in the GATT. Additionally, the foreign sales

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2. These other significant activities might include:

   a. disbursement of export related advertising expenses;
   b. maintenance of separate bank account;
   c. maintenance of paid in capital;
   d. holding directors' meetings;
   e. holding shareholders' meetings;
   f. disbursement of dividends;
   g. disbursement of legal fees;
   h. disbursement of accounting fees;
   i. disbursement of officers' salaries;
   j. disbursement of directors' salaries;
   k. communicating with the general public; and
   l. transfer of title.

corporation can only be located in a territory or country which has an exchange of information agreement with the United States.

VI. TAXATION OF U.S. SHAREHOLDERS OF FOREIGN CORPORATION

The tax exempt portion of FTI will not be included in the income of a U.S. shareholder under subpart F. In addition, U.S. shareholders will be allowed a 100 percent dividends received deduction with respect to actual dividends from earnings attributable to tax exempt FTI. The dividends received deduction will be in lieu of a foreign tax credit. Other earnings will remain subject to the existing U.S. tax regime, including the subpart F and foreign tax credit rules.

VII. REVENUE NEUTRAL CAP ON THE TAX EXEMPT BENEFIT

The CCCT specified that the proposed alternative should cost no more than the DISC in terms of lost tax revenue. For taxpayers using an administrative allocation rule, the amount of tax exempt FTI will be limited to the greater of 17 percent of the combined taxable income of the foreign corporation and its related supplier; or 1.35 percent of the foreign corporation's gross sales, but not to exceed 34 percent of combined taxable income. If the foreign corporation purchases goods from an unrelated party or determines its transfer prices under the Section 482 regulations, the limit on the tax exempt benefit will be equal to 34 percent of the foreign corporation's FTI.

VIII. SIMPLIFICATION

Under the proposal, the tax benefit conferred on FTI is an exemption from U.S. tax on income attributable to foreign economic processes. The proposal eliminates conditions on the tax benefit such as the requirement under DISC that tax deferred income be invested in certain assets. The tax exempt funds can be made immediately available to U.S. shareholders of the foreign corporation tax free, without the necessity of complicated producer's loan type limitations.

The elimination of the asset requirement also avoids the problems presently associated with accumulated DISC income. Complicated "recapture" provisions for accumulated FTI will be unnecessary. The simplification of the measure will help offset the burden of conducting activity outside of the United States, particularly for small businesses.

IX. SMALL BUSINESS OPTIONS

Small businesses will be given the option of choosing either to pay an interest charge on deferred taxes or to participate in jointly owned foreign sales corporations.

a. Interest Charge Alternative

Under this alternative, exporters would be allowed to continue to operate their DISC's for sales of up to $10 million. An annual deductible interest charge would be imposed on the value of the tax deferral at the Treasury bill rate. The current pricing rules would remain in effect, but the deemed distribution and incremental provisions would be eliminated. Thus, up to 100 percent of the DISC income covered by this alternative could be deferred. This would be necessary to make the approach attractive in light of the additional cost associated with the interest charge.

b. Joint Participation

This option would allow for the formation of foreign sales corporations on a joint basis. Participation would not be limited by type or size of firm. Non-profit entities such as state development corporations and port authorities could be used as the vehicles for foreign incorporation. The joint participation could extend to both usage and ownership so that participants would receive distributions on a patronage basis.

X. TREATMENT OF ACCUMULATED DISC DEFERRAL

The proposal envisions the repeal of the current DISC provisions of the Code. The accumulated deferral income will not be subject to taxation under this proposal.

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FOR IMMEDIATE RELEASE
Friday, March 11, 1983

STATEMENT BY DONALD T. REGAN
SECRETARY OF THE TREASURY
MARCH 11, 1983
WASHINGTON, D.C.

Today the Senate is considering an amendment to the jobs bill that would repeal the new requirement for withholding of taxes on income from dividends and interest.

The withholding provision of the 1982 tax bill was adopted to improve the collection of taxes already owed the government. We felt it was far better to collect the more than $20 billion already owed over the next five years than to impose new taxes. Withholding is a tried and true system that for nearly 40 years has proven an effective means for collecting taxes on wages and salaries.

Yet today we see a massive lobbying campaign by the banking and savings and loan industry to promote special interest legislation. They have flooded their customers with literature, much of which is irresponsible and untruthful, claiming that the government is trying to take their savings. Bold headlines proclaim that savings will disappear. Form letters to depositors say withholding will take food off their table. Television ads don't even veil the attempt to scare older people. All of these efforts add up to an incredible performance by the banking industry for its own private gain, at the expense of all honest taxpayers.

This is an industry that calls for reduced deficits, but wants someone else to pay the bill. They pay little taxes themselves, yet want others to pay more taxes rather than collect those already owed. They express concern for their depositors, but hold up a jobs bill that helps the unfortunate workers who are unemployed.

Today the Congress stands knee deep in cards and letters from frightened citizens who have been misled by this campaign. And it's to those people that I want to be very direct in saying: this is not a new tax. It will not take your savings. Over 85 percent of older citizens are exempt. Exemptions are easy to get. Last year your congressional representatives acted with foresight and courage in passing this law which makes everyone pay what is due. The law should be preserved.

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For Release Upon Delivery
Expected at 10:00 a.m. EST
March 11, 1983

STATEMENT OF
WILLIAM S. MCKEE
TAX LEGISLATIVE COUNSEL
DEPARTMENT OF THE TREASURY
BEFORE THE SENATE FINANCE COMMITTEE

Mr. Chairman and Members of the Committee:

I am pleased to have this opportunity to discuss the current rules governing the taxation of depository institutions. We think it is appropriate and timely to review the tax treatment of all financial institutions and their products given the significant changes in the financial services industry in recent years.

Background

Any tax legislation affecting depository institutions and their products should reflect the significant changes that have occurred recently in the operation of all financial institutions. Financial deregulation measures, such as the Garn-St. Germain Depository Institutions Act of 1982, have expanded the powers of banks and thrift institutions. In addition, the life insurance industry has developed new products that contain predominantly investment features similar to those offered by depository institutions. As a consequence of the increasing similarity of products offered by different financial institutions, the tax treatment of the institutions and their products can greatly influence their relative competitive positions.

The taxation of financial institutions is also particularly important as we pursue our commitment to encouraging long-term savings which are essential to the continuation of our economic recovery. The rate of return to savers and the relative efficiency of the use of the savings are affected by the taxation of the financial institutions through which a major portion of all savings flow. Different tax rules for financial institutions and their products may also reduce and distort the flow of savings from their most productive uses.

While we have not completed our review of the tax treatment of depository institutions and other financial institutions and their products, we are prepared to discuss some of the general considerations which should be part of such a study. First, I will briefly describe the major provisions of current law affecting the tax treatment of depository institutions and their products.

Current Tax Rules Affecting Depository Institutions and Their Products

General

Depository institutions generally are subject to the corporate income tax. Credit unions are an exception and are exempt from tax on their income, regardless of whether retained or distributed to depositors as dividends. When savings and loan associations and mutual (nonstock) savings banks became subject to the corporate income tax in 1951, credit unions were not made taxable despite their similarity to other thrift institutions. However, in 1951 credit union deposits represented a relatively small share of total savings. Since that time, credit unions have grown rapidly, partly as a result of their tax-exempt status.

Significant General Tax Rules

Before describing the special tax rules applicable only to depository institutions, I should make note of two aspects of the Internal Revenue Code which are not limited to depository institutions but which significantly affect the tax liabilities paid by depository institutions. It is important to understand that these two provisions are available to all taxpayers.

First, the interest on State and local government obligations (including certain industrial development bonds issued for private businesses) is exempt from tax. Close to half of the new tax-exempt bond issues in 1982 were for private purposes, such as owner-occupied housing, pollution control, student loans, private hospitals, and private businesses. Commercial banks are among the primary investors in tax-exempt bonds. Second, the investment tax credit and accelerated cost recovery ("ACRS") allowances reduce the tax liabilities of depository institutions as a result of their participation as lessors in leasing arrangements.

Special Rules for Depository Institutions

Deduction for Interest Paid. Financial institutions differ from nonfinancial businesses in their heavy reliance on debt capital. Most of the funds employed by financial institutions are provided by creditors (depositors or policyholders), rather than by shareholders. The amount of equity capital as a fraction of total assets in most financial institutions is only 5-10 percent, compared to 40-60 percent for most nonfinancial businesses. Thus, the most important deduction is for interest paid (and, in the case of thrift institutions, dividends paid or credited on withdrawable accounts), which accounts for 60-65 percent of total expenses.

Generally, interest deductions are not allowed for debt attributable to purchasing or carrying tax-exempt securities. Prior to the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), the interest paid by commercial banks to depositors was specially treated in that it was generally not considered to be incurred to purchase tax-exempt bonds. As part of a general cutback on corporate tax preference items, TEFRA disallowed 15 percent of the interest deduction on indebtedness incurred by commercial banks to purchase or carry tax-exempt obligations acquired after 1982. Other businesses, such as security dealers, whose businesses involve carrying tax-exempt obligations cannot deduct any interest paid to purchase or carry those bonds.

Deduction for Additions to Bad Debt Reserves. Unlike nonfinancial businesses, depository institutions can deduct additions to reserves for bad debts using a method totally unrelated to the actual experience of the taxpayer.

Commercial banks can choose either the percentage or the experience method for determining their bad debt deduction. The percentage method allows a current deduction for additions to reserves sufficient to maintain a reserve of up to 0.6 percent of eligible loans outstanding. The experience method generally is based on average loan losses over a six-year period. Banks need not use one or the other method consistently. The election to use the percentage method is scheduled to expire at the end of 1987, at which time all commercial banks must use the experience method.

Thrift institutions may use modified versions of the percentage method or the experience method available to banks. Alternatively, thrift institutions, if they hold sufficient amounts of their assets in certain eligible investments (primarily residential mortgages), can elect the percentage of taxable income method for purposes of establishing their bad debt reserves for qualifying real property loans. Savings and loan associations and stock savings banks must hold at least 82 percent of their total assets in eligible investments to be able to claim the maximum deduction, which is equal to 40 percent of taxable income (computed with certain modifications). The deductible percentage of taxable income is reduced if fewer than 82 percent of total assets are eligible investments. Mutual savings banks must hold at least 72 percent of their total assets in eligible investments to take advantage of the maximum deduction, which is also subject to reduction if the percentage of eligible investments declines below 72 percent. As a result of the deduction allowed under the percentage of taxable income method, thrift institutions that can claim the maximum deduction are subject to a maximum marginal tax rate of only 27.4 percent, since they pay tax on only 60 percent of their taxable income at a maximum rate of 46 percent.

Thrift institutions that qualify for the percentage of taxable income deduction are limited in the amounts of certain other tax benefits they may claim. For example, thrifts are entitled to only half of the otherwise allowable investment tax credit, and they receive a scaled back dividends received deduction compared to that available to other corporations.

The minimum tax provisions of TEFRA include a cutback of the amount of bad debt reserve deductions of depository institutions. Fifteen percent of the addition to bad debt reserves in excess of those allowable on the basis of actual experience is disallowed. Additionally, 71.6 percent of the the addition to bad debt reserves in excess of the the addition that would have been allowed based on actual experience is a tax preference item for purposes of the corporate add-on minimum tax.

The appropriate tax treatment for additions to reserves for future contingencies such as bad debts is an important issue in the tax treatment of financial institutions. In order to be neutral, the use of reserve accounting for tax purposes should be equivalent to the deduction of actual losses when they occur. The current deduction for additions to reserves by depository institutions and insurance companies may overstate the present value of the future expected losses and thus understate real income.

Other Special Provisions for Depository Institutions. A number of other special provisions in present law apply to depository institutions. Unlike most other taxpayers who are permitted to carry back net operating losses for only three years, commercial banks and thrift institutions are allowed a 10-year net operating loss carryback period (but are limited to a 5-year carryforward period rather than the 15 years generally allowable). This means that depository institutions may be able to claim refunds resulting from losses sooner than other taxpayers.

Mutual thrift institutions are allowed to deduct the full amount of interest or dividends paid or credited to withdrawable accounts, even though some of the dividends or interest may be paid to depositors out of a return on equity capital in their capacity as owners of the mutual institution. The return paid on equity generally is not deductible under our corporate tax system.

In addition, a series of special rules has been enacted to relieve tax liabilities or other burdens that would otherwise be imposed in case of mergers involving financially troubled thrift institutions.

The Tax Treatment of Depository Institution Products. The effect of the tax system on depository institutions is also determined by the income tax treatment of their products. The income credited on investments in bank and thrift deposits is generally subject to tax when earned, unless it is exempted for certain well-defined policy reasons. For example, the investment income earned on tax deductible contributions to qualified retirement plans and individual retirement accounts is effectively untaxed in order to encourage savings for retirement. It should be noted that these tax-favored forms of savings are available from all financial institutions. The All-Savers Certificate, which expired at the end of 1982, was an exception in that it was available only from depository institutions.

The income from investments which are offered jointly with financial services, such as checking account services, is often reported net of the income attributable to the value of the services. This is comparable to the deduction of the payment of the cost of those services. When financial services are unrelated to earning investment income, the costs of those services are similar to personal expenditures which would normally not be deductible. Thus, where investment income is reported net of the cost of personal expenses, nondeductible personal expenses are effectively converted to deductible expenses. Financial institutions that can offer tax-favored checking accounts and other personal services with their investment products can offer higher after-tax total returns and thus can attract more savings than other financial institutions.

Effective Tax Rates on Financial Institutions

Several studies have been published that show effective tax rates on commercial banks to be among the lowest for all industries. As conventionally measured, effective tax rates generally compare a taxpayer's taxes paid with its income reported on its financial statements for a given year. These measures indicate the extent to which the tax system is used to provide incentives for numerous social purposes, rather than to raise revenue at the statutory rates. At a time of fiscal austerity and large projected future deficits, the benefits from tax credits, deductions, and exemptions that cause low effective tax rates should be carefully reviewed to insure that the original purpose still merits this form of government assistance.

Conventional effective tax rates are significantly below the maximum statutory corporate tax rate in almost all industries. The Joint Tax Committee study, prepared for Representatives Pease and Dorgan, shows a ratio of U.S. taxes paid to current U.S. source income of 2.7 percent in 1981 for 20 large commercial banks. This indicates that a large amount of tax subsidies for a variety of purposes are passing through the commercial banking sector.

As previously explained, certain tax law provisions of general applicability to all taxpayers are heavily used by depository institutions to reduce their tax liabilities. In addition, there are other provisions that are peculiarly applicable to banks and thrifts. In the case of thrift institutions, examples of the latter provisions include both the tax exemption of credit unions, which reduces their effective tax rate to zero, and the percentage of taxable income bad debt reserve deduction, which reduces the maximum effective (and marginal) tax rate of other thrift institutions to 27.4 percent. In the case of banks, interest paid to depositors is deductible even though the borrowed funds are used to carry tax-exempt bonds which can reduce a bank's effective rate substantially below 46 percent. In addition, deductions for additions to bad debt reserves are available in amounts that may exceed bad debt losses determined on the basis of actual experience or expected future liabilities.

Some of the benefits of these special tax rules, such as the bad debt deduction allowable to banks, may inure primarily to the benefit of the financial institutions. Other benefits are shared with or transferred to others, such as State and local governments and IDB users that benefit from lower interest rates on tax-exempt bonds held by banks.

As I have mentioned, conventional effective tax rates can show the total amount of tax subsidy as compared to statutory tax rates. However, comparisons of those effective rates across industries cannot, in many cases, indicate which industries bear a lower direct economic burden from the tax system than others. The direct economic burden borne by taxpayers as a result of the income tax system cannot be measured simply by measuring taxes actually paid. This is because the tax system causes reductions in disposable income and creates differences between pre-tax and after-tax returns by means other than the direct assessment of taxes.

It is important in the case of banks to recognize that tax rules directly reduce the yields on tax-exempt bonds and the rentals on leased property. These market adjustments are what provide the subsidy to users of tax-exempt bond proceeds and lessees. For example, the tax exemption of interest paid on State and local government obligations increases the demand for them, which raises their purchase price and lowers the market yield below yields on comparable taxable securities. The lower yield on tax-exempt bonds accrues to State and local governments and IDB users in the form of lower interest costs, but that lower yield reduces the benefit of tax exemption from the point of view of bank shareholders. Thus, the low tax rate of investors in tax-exempt securities is a result of tax subsidies that accrue largely, but not entirely, to tax-exempt issuers.

If the pass-through of the subsidy is relatively efficient then most of the tax benefits will accrue to the intended beneficiaries. In the case of short-term tax-exempt bonds, the subsidy mechanism is usually fairly efficient. The percentage reduction in yield (and rate of subsidy) for most short-term tax exempts is reasonably close to the maximum statutory corporate tax rate of 46 percent plus the applicable net marginal State tax rate, so State and local government issuers receive most of the subsidy. In these circumstances, banks receive little more than the cost of the services provided. Tax-exempt bonds with longer maturities offer a lower rate of subsidy to tax-exempt issuers, since their yields range from 60 to 85 percent of taxable yields of comparable securities. Long-term tax-exempt bonds are thus quite inefficient subsidy mechanisms because the intended beneficiaries receive only between one-half to three-quarters of the lost Federal revenue, with the remaining subsidy captured by investors. The inherent inefficiency of the tax-exempt market and the concomitant benefits received by banks could be eliminated by providing the subsidy to State and local governments and IDB issuers directly in the form of cash grants.

An alternative calculation of effective tax rates for banks could be attempted that would remove the subsidy element that benefits tax-exempt bond issuers and lessees and would only include the subsidy that benefits banks. Such a measure would show the differences in the cost of raising equity capital for banks as compared with such costs for other kinds of businesses. This measure of the effective tax rate would recognize the pass-through of tax benefits which typically occurs when the ultimate beneficiary pays a lower return to the financial institution because of the tax benefits. This measure of the relative tax burden across industries would restore the amount of benefits transferred to the ultimate beneficiaries to both the numerator and the denominator of the effective tax rate fraction.

The necessary adjustments in the computation of the effective tax rates of the largest commercial banks would clearly raise their effective tax rates significantly above the estimates given by conventional ratios of tax payments to book income, but they would remain well below the statutory tax rate of 46 percent. The alternative measure of the effective tax rate removes the subsidies that do not accrue to banks and focuses on the tax subsidy that banks actually receive.

Because of their major role as a tax intermediary, we would expect an alternative effective tax rate calculation to show that shareholders of commercial banks do not derive significantly more tax benefits than shareholders of other industries. Tax incentives that are available to all taxpayers should tend to equalize the cost of raising equity capital across industries. Only where the tax benefits are limited to a particular industry, such as the banks' preferential interest deductions, the thrifts' special bad debt deductions or the credit unions' tax-exempt status, would relative tax burdens be expected to vary greatly.

Even though an alternative effective tax rate analysis would probably show that banks are not capturing more tax benefits than other sectors of the economy, it must be remembered that large amounts of tax subsidies are being passed through banks to other beneficiaries. Clearly, this large leakage of revenue is a cause for concern if the subsidies are inefficiently delivered through the banks or the subsidies are benefiting activities that do not merit government assistance.

In summary, two points must be kept in mind. First, there are large amounts of subsidies that are currently being delivered through the tax system. The low conventional effective tax rate paid by large banks raises the question of the propriety of such large subsidies hidden in the tax system. For example, we question whether the large volume of private purpose IDB's, which account for roughly half of new tax-exempt bond issues, should continue to be a drain on Federal tax revenue and reduce the taxes paid by investors in tax-exempt bonds, such as commercial banks.

Second, conventional effective tax rates do not show who actually benefits from the subsidies. An alternative calculation is needed to compare the relative burden of the tax system across industries, because many of the tax benefits are passed through to nontaxpayers.

Tax Incentives and the Minimum Tax

One response to low effective tax rates has been an expansion of the minimum tax provisions. It must be recognized that, in most instances, the minimum tax reduces the extent to which taxpayers make use of the existing tax incentives. This reduces the amount of the subsidized activity or the amount of the subsidy received by the intended beneficiaries. Thus, a minimum tax must balance the concern with fairness and the desired amount of the tax incentives.

This tradeoff can be seen in the case of the tax preference cutback on banks' interest deductions for holding tax-exempt bonds. The effect of the cutback on the interest deduction incurred for carrying tax exempts will initially reduce banks' demand for tax-exempt bonds. This will reduce the Federal subsidy inherent in tax-exempt financing by raising the interest rate that eligible borrowers have to pay to a rate closer to that paid by all other borrowers.

A comparison of the two changes in TEFRA affecting tax-exempt bonds is instructive. The tax preference cutback provision indirectly reduced the incentive provided to issuers of tax-exempt bonds by reducing the interest deductions allowed commercial banks. TEFRA also included a number of direct limitations on the use of tax-exempt bonds for private purposes. The limitations on industrial development bonds included reducing the double-dipping of tax benefits by private users of tax-exempt bond proceeds and requiring public approval of the bond issues to insure that they serve a public purpose. The bank preference cutback reduces the subsidy to all tax-exempt bond issuers, while the IDB restrictions are targeted at private purpose tax-exempt bonds and would actually improve the rate of subsidy for the remaining State and local public purpose issuers.

Conclusion

The relative tax treatment of financial institutions and their products will become increasingly important as financial deregulation and other developments make these different institutions more alike in the financial services they provide. The issues raised in these hearings deserve careful analysis and consideration. The Department of the Treasury would like to work closely with the tax-writing committees on a comprehensive review of the tax treatment of all financial institutions and their products, and a review of the existing subsidies provided through the tax system.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 12:00 NOON March 11, 1983

TREASURY'S 52-WEEK BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for approximately $7,750 million of 364-day Treasury bills to be dated March 24, 1983, and to mature March 22, 1984 (CUSIP No. 912794 EE 0). This issue will provide about $ 2,475 million new cash for the Treasury, as the maturing 52-week bill was originally issued in the amount of $5,277 million.

The bills will be issued for cash and in exchange for Treasury bills maturing March 24, 1983. In addition to the maturing 52-week bills, there are $11,496 million of maturing bills which were originally issued as 13-week and 26-week bills. The disposition of this latter amount will be announced next week. Federal Reserve Banks as agents for foreign and international monetary authorities currently hold $ 1,712 million, and Federal Reserve Banks for their own account hold $ 3,936 million of the maturing bills. These amounts represent the combined holdings of such accounts for the three issues of maturing bills. Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average price of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them. For purposes of determining such additional amounts, foreign and international monetary authorities are considered to hold $505 million of the original 52-week issue.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. This series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Thursday, March 17, 1983. Form PD 4632-1 should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

R-2079

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders, the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids.

Settlement for accepted tenders for bills to be maintained the book-entry records of Federal Reserve Banks and Branches st be made or completed at the Federal Reserve Bank or Branch March 24, 1983, in cash or other immediately-available funds in Treasury bills maturing March 24, 1983. Cash adjustments ll be made for differences between the par value of the maturing lls accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the ount of discount at which these bills are sold is considered to crue when the bills are sold, redeemed, or otherwise disposed of. ction 1232(a)(4) provides that any gain on the sale or redemp- on of these bills that does not exceed the ratable share of the quisition discount must be included in the Federal income tax turn of the owner as ordinary income. The acquisition discount the excess of the stated redemption price over the taxpayer's sis (cost) for the bill. The ratable share of this discount determined by multiplying such discount by a fraction, the merator of which is the number of days the taxpayer held the ll and the denominator of which is the number of days from the y following the taxpayer's date of purchase to the maturity of e bill. If the gain on the sale of a bill exceeds the taxpayer's table portion of the acquisition discount, the excess gain is eated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - s. 26-76 and 27-76, and this notice, prescribe the terms of ese Treasury bills and govern the conditions of their issue. pies of the circulars and tender forms may be obtained from any deral Reserve Bank or Branch, or from the Bureau of the Public bt.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

REMARKS BY
THE HONORABLE R. T. MCNAMAR
DEPUTY SECRETARY OF THE TREASURY

BEFORE THE
EASTERN ECONOMIC ASSOCIATION
BOSTON, MASSACHUSETTS
MARCH 10, 1983

I have some good news and some bad news. The good news is that I am not an economist. The bad news is that I think economists are important and should be listened to. I listen -- especially to economists who don't live in Washington. The reason is simple. Those who live in Washington know all the answers without knowing the issues or doing any analysis.

Not being an economist, I come to you in the role of a consumer, a consumer of your "good" advice and "sage" counsel. Rightly or wrongly, it's my job to help implement in a pragmatic fashion a set of government policies and programs for economic progress suggested by your theories and research. Thus, I bring you a report from the field, and as a consumer just perhaps a consumer complaint or two.

Now, in fact, there are other considerations in policy development than economic theory. Policy will be made and implemented in the capitals of the world with or without economic research and expert guidance. If you need proof only look at our history on energy legislation. Time, tide, and political whirlwinds wait for no man -- not even Professor Galbraith, who I presume is still pontificating. But economic policy made with expert input is at least apt to be better, if only at the margin, than policy made without expert input. Thus, the economics profession has a future.

Thus, it was with great pleasure that I learned only last week that there might be -- in the attic of the Main Treasury Building -- a time capsule, placed there twenty years ago in 1963 by Professor Walter Heller, after the discovery of the new economics of the '60s. We didn't find one. But if we had, let me suggest some of the material it would have contained from all schools of economic thought.

R-2080

FINE-TUNING

The "new" economics of the 1960s, according to the capsule, was the last word in economic science. Indeed, it was the last word we would need from economists. It would eliminate the business cycle and usher in perpetual prosperity by fine-tuning the economy. But the economy in the 1970s was not "fine-tuned" -- it ended up "highly strung." And if many nervous economists and embarrassed forecasters wished the 1970s had never happened, that was as nothing compared to the hysteria in Washington.

The question for today, and perhaps tomorrow, is can the economy be fine-tuned? The Reagan Administration doesn't think so.

We've tried to develop and stick with a long-term program of fundamental fiscal, monetary and regulatory tax reform for the decade. We didn't and don't have a magic wand. Not only don't we have all the economic answers, we're still trying to identify all the coefficients. And, we aren't any smarter than the average human, despite what some members of our own Administration think of themselves. The long view was a constant feature of our overall policies. Policy should not be based on the morning edition of the *Washington Post*. In sum, short-term politics shouldn't determine long-term economic policies.

Do we have the tools to fine-tune the economy?

The economic impact of budget outlays and receipts is properly measured, according to traditional theories, by the government sector of the national income and product accounts. But this is not the same as the unified budget used by government or it used to be used by the government. We haven't passed a budget since fiscal year 1977. The unified budget outlay, receipts and deficits cannot be the relevant policy tools for fine-tuning. Or can they? Is that their purpose? Using the Federal budget as a tool for policy fine-tuning is like doing major surgery with a monkey wrench.

Even if the unified budget were the proper tool, could it be employed in a useful way? Hardly. Consider that the budget for any fiscal year is supposedly designed almost a year ahead, submitted eight months ahead, and passed several months ahead of the start of the fiscal year. Forecasting economic conditions 12 to 24 months ahead is a fine art at best. Many forecasters over the last few years could not even predict the direction of the GNP in the quarter in which the forecast was made. There is little likelihood that the budget would perfectly fit the conditions a year in the future if you wanted to fine-tune the economy.

Indeed, the converse is true. It is more likely that
›nditions would mold the budget. The President's budget is
ıanged by Congress in the First Budget Resolution; it may be
ıanged again in the Second Budget Resolution, if there is a
cond Resolution; and when the Second Resolution proves to be
ıconvenient during the appropriations process, as it invariably
›es, there may be a retroactive Third or Fourth Resolution.
ıese accommodate supplemental spending due to Congressional
ərgesse, Administration requests, automatic entitlement growth,
r to allow for a recession-related revenue drop. To put it
ildly, the budget process bears but a passing resemblance to its
extbook portrait.

But how about traditional deficit spending bills?

Then there are the inevitable delays even with targetted
ingle bills. The economic textbooks always pay lip service to
wo kinds of lags. First, there is the delay between the
mergence of an economic problem and recognizing it and
mplementing an appropriate policy change. This is called an
nside lag. Politicians like generals can only look backwards
ot think ahead. Thus, like fighting the last war, politicians
oo often work on the problems of the past, not the present or
he future.

In addition, in économic policymaking there is the delay
etween implementation of a policy change and the time it begins
o have an impact on the economy, called an outside lag. The
nside lag is a political problem. The outside lag is an
conomic problem. Both are policy problems. Yet, the economic
iterature is sparse at best on these key issues.

I often wonder if the economic advice we receive takes these
ags fully into account. It sometimes seems that our form of
overnment, with its cumbersome separation of powers, two-house
egislature and committee system, just cannot develop legislation
s quickly as, perhaps, a parliamentary system. This may be good
n balance, but considering the quality of much of what the
overnment does, it can create problems for those who would have
ıs intervening constantly in the economy to fine-tune it.

Consider, the current jobs bill is a case in point. The
›ressure in Congress for a jobs bill came with a supposed
lovember mandate, geared to the election calendar, not to the
conomy cycle. There are two broad concerns with jobs bills.
'irst, most increase spending and don't create net gains to the
conomy or provide permanent employment. But, they will increase
he deficit and therefore Treasury borrowing. The second is the
ag effects. It may produce a March authorization, a June
ıppropriation, and a fiscal 1984 implementation which, under
›rdinary circumstances, should put the impact entirely within the
econd year of an increasingly robust recovery which appears to
ıave begun in December 1982.

There is little that can be done now to avoid the institutional inside lag associated with a jobs bill. However, to make the effect of the jobs package occur sooner, to move the attendant Treasury borrowings from 1984 to 1983 to the extent possible, we have simply accelerated already authorized Federal construction projects as the basis for the jobs bill. By moving ahead early with budget projects already planned and approved, we should be able to minimize delays in implementation and receive as much of the benefit of the bill as possible in the summer of 1983. The added advantage, of course, is that the impact on the deficit will be shifted forward to a time of relatively slack private loan demand. In other words, we will borrow this year not next. This situation is not unique. Indeed, even a March appropriation would get legislation into law only one quarter after the end of the downturn, something of a record. The recession which ended in February 1961 also spawned a public works bill. It was passed in September 1962. The 1970 recession produced a public works bill. It was passed in 1972. The 1973-75 recession generated two public works bills. One year later, in 1976, and two years later, in 1977. Hence, the current jobs bill should be substantially better than our previous "fine-tuning" efforts.

I was not always skeptical of fine-tuning. I have fond memories of my <u>first</u> stint in Washington as a member of the Pay Board of the Cost of Living Council. I came because inflation was over 5 percent and I thought wage-price controls would lower it from that level. Well, we fine-tuned <u>everything</u>, with gusto. But somehow the result of our fine-tuning was more "discord" than harmony. So we are not attempting to fine-tune fiscal policy anymore. And, although my <u>second</u> stint in Washington is certainly not without discord, at least the restaurants in Washington are minimally better than 10 years ago.

Well, if we can't fine-tune with fiscal policy, can we fine-tune it with monetary policy? The Keynesians in my Treasury time capsule told us years ago that money doesn't matter. More recently they have been saying that it doesn't matter much. After 1979 when the Fed declared itself to be monetarist, the Keynesians seemed to think it mattered a bit after all. Meanwhile, Milton Friedman, after assuring the world both before and after 1979 that any resemblance between Fed policy and the policy of any monetarist is non-existent, said that money matters a lot in the short run for real output, but that monetary policy involves longer inflation lags, and is too clumsy and unpredictable to be used for fine-tuning. In the long run, if money only creates inflation, not real growth, and is generally useless as a means of fine-tuning employment, should it matter? In fact, if inflation drives interest rates and tax rates higher, is it better to set money growth at a long-run, non-inflationary rate and forget the whole thing?

MONETARY POLICY

The Reagan Administration thought money did matter. As you e aware, we asked the Fed to move smoothly and gradually to a n-inflationary money growth rate. This brought up a surprising mber of questions, which looked so simple that any layman like self might be forgiven for assuming they had already been swered. I searched your economic literature for the answer.

First, what is money? Surely, after 5,000 years of vilization, 200 years since David Hume, and roughly 20 since ie Friedman-Samuelson debates, we should have a better answer ian "money is anything which is accepted as such."

Second, what is a smooth gradual adjustment? Is moving from percent money growth to 5 percent in one year different from)ing it in four years? Is 5 percent money growth the same if it ; 5 percent each quarter, as opposed to 14 percent January ırough April, only 1 percent May though September, 7 percent in :tober and November, and 15 percent in December and January?) you want a basketball team averaging six feet with one at nine eet and four at five feet?

These simple questions have given us a whole new vocabulary: ıflation premiums, volatility or risk premiums, shift evel adjustments, M1-A, M1-B, old M1, new M1, old and new M2, ıd so on.

My favorite new word is "velocity." You economists were so uch help on this last year. Now, in my twenty year old time apsule I found a lot of debate over velocity. Some said it andered randomly and without constraint. Others said it never oved. (I won't ask what you individually said.)

In the early days of the Reagan Administration, Treasury ook the view velocity was somewhat elastic and somewhat redictable, but not so elastic as implied in our first so-called rosy scenario." We were overruled there by those who placed heir bets on "core inflation" and high nominal GNP in spite of he Fed's announced money slowdown.

In any event, as inflation has come down even faster than reasury predicted, and confidence in the dollar has risen, elocity has fallen, allowing a bit more leeway from money rowth.

The idea goes like this: Print too much money and inflation will go up -- unless velocity goes down. That is, if people are trying to rebuild their money balances because of renewed confidence because inflation is falling, because less money is being printed, then more money will have to be printed. Otherwise, we will have deflation. Who here today has written a monograph in the relationship, if any, of velocity of money to core inflation? And who has examined consumer preference to hold liquidity when unemployment rates are over 10 percent?

It would be extremely helpful to those of us who must live in Washington to have a better understanding of velocity. For example, how much does velocity move reactively to exogenous changes in money growth, falling in the short run to offset a burst of money creation, or rising to make a tight money supply go further? How much does velocity move actively on its own response to oil or political shocks, or to changes in inflationary psychology, implying the need to adjust money growth to offset the velocity shift?

Monetary research has never been more important than today. In this recent recession, monetary policy has again demonstrated its power relative to fiscal policy. Our goal is stable prices, steady growth of output at a sustainable rate (which we would like to improve upon) and low interest rates. Yet, when we ask the basic question, "Will faster money growth make interest rates go up or go down?" the answer comes back a definitive, "yes." Unfortunately, that is not exactly the sort of answer we would find most useful. But keep those monographs coming folks!

All of this brings up the question of what the Fed should aim at. Should it operate on a quantity rule, stabilizing the growth rate of money? Should it develop a price rule? Should a price rule be indirect, adjusting money growth rates to counteract swings in some measure of general prices or in the prices of a group of selected commodities? Should a price rule be direct, with actual intervention in commodity markets a la a gold standard? An interest rate rule is often suggested by Congress, but with all those inflation and volatility premiums and psychological crosscurrents, the danger of mixed signals and perverse policy moves seems to be too strong. Or can an interest rate rule be developed in spite of its problems?

In fact, we do know that inflation drives interest rates over longer-term periods. But, while there is much evidence to suggest that deficits and interest rates are systematically linked, there is enough conflicting empirical data to suggest that we do not yet adequately understand the link between deficits, money growth, inflation, and interest rates.

What really is the measure of fiscal impact on interest rates? Is it the deficit per se that causes high interest rates? Or is it the degree to which the Fed is anticipated to accommodate the deficit with faster money growth that causes rates to go up? There are even some studies that suggest that the level of government spending has more impact on interest rates than the gap between government outlays and receipts.

As for the deficit, what is the appropriate measure of its pact? Obviously, the deficit must be compared to the "pool of vings" available to finance it, since saving plus taxes equal e amount of GNP not consumed by the private sector, and thus 'ailable for government use.

But what is the appropriate savings pool? Some compare the ficit to the flow of funds in financial markets. But the flow : funds varies in importance for investment and growth as firms .nance more or less of their investment internally. Some mpare the deficit to net national savings. But depreciation d gross savings are also available for investment as well. ideed, much repair and replacement of capital equipment is inanced by tax deductible spending on maintenance, which is in ldition to the capital consumption allowances. Is it perfectly lear that gross savings merely replace existing stock and net ew investment and savings are required for net new capital kpenditures?

Ultimately, of course, no country is an island, at least not inancially. The U.S. deficit, and U.S. investment, are financed n a world capital market which is several times the size of the .S. capital market. Witness the substantial increase in recent ears in foreign direct investment in the U.S.

THE DEFICIT AND INTEREST RATES

We are all concerned that budget deficits could, if onetized, cause inflation. However, recently deficits have not een excessively monetized, and the inflation rate has come down. ut it if is to stay down, the Fed must not now become overly xpansive just because the wind has shifted. It must lean gainst the wind, but it should not lean so hard into the revailing gust that it forgets where the previous gale came rom.

This brings me to the concern that unmonetized deficits ould force interest rates so high as to abort the recovery. I or one am uncertain that they inevitably will, for two reasons. 'irst, short term, the deficits are due in large part to 'ecession. Second, long term, I believe that deficits will be rought down, by real economic growth and moderate spending 'estraint, and that the Federal Reserve will be able to walk the 'ine line which will promote recovery while bringing inflation nd interest rates down further.

Certainly recent history shows that high interest rates and igh deficits are not necessarily always perfectly coincident. etween August 1981 to August 1982 estimates of the deficit oubled and tripled, but nominal interest rates fell ubstantially during the recession. Yet, real interest rates ncreased substantially. I must ask you, the experts, why? Was t all the recession?

It is puzzling, if deficits influence interest rates, how this fall in rates could have occurred. Clearly, the steepest post-World War II recession and lower inflation were major contributing factors. But, even more surprising is the size of the interest rate decline since August 1982. On September 1, 1982, the CBO increased its FY 1983 deficit projection from $118 billion to $150 billion, and Solomon Brothers forecast an FY 1983 deficit of $178 billion. The Administration's budget forecasts a 1983 deficit of $208 billion. Yet the rally continued in the bond markets. Why?

In my view, we must look to renewed confidence in the Fed and good news on the inflation front for partial explanations, as well as to the growing realization that a stronger-than-predicted economic recovery will help to close the budget gap. Clearly, this is an area needing more research.

TAX THEORY

Well, if I have questions on macro-economics, let's turn to tax theory. Here there are certainly different theories of taxation.

Do tax changes affect the economy primarily by pumping money in or taking money out? Those who view spending as the true burden of government, as the real measure of resource absorption, would say no. They would say that taxes, or borrowing that implies future taxes, are just two different ways to finance spending, and that there is no stimulus from shifting back and forth.

If this is true, do taxes matter? The neoclassical approach says yes, insofar as they affect relative prices, the neoclassical approach. This leads to questions involving savings behavior, labor force impact, the underground economy, flat rate tax vs. progressive tax, income tax vs. consumption tax. I suggest all have been woefully underinvestigated. In fact, the single best piece of research in this area may be the Treasury's "Blueprint for Tax Reform," done in 1975, and released in January 1976 by Secretary Simon. Isn't there any better or more current literature than that?

We need to take a look at the double or triple tax treatment f dividends, capital gains, and savings income in general under ur mixed system of corporate and personal income taxes. Serious ork by the economics profession needs to be done on the concepts f a broader-based, flatter-rate income tax, or possibly a more eutral integrated consumption tax. Here the political side of olitical economy comes into play. Imagine, just as the tip of he iceberg, the opposition to the loss of specific deductions by omebuilders' associations, S&Ls, or charities under a truly roadened tax base, even if current recipients were somehow randfathered! Indeed, what is a so-called tax expenditure? hat are their economic impacts? I for one would like to know.

Nonetheless, as policymakers, we need to analyze the impact f high marginal tax rates on savings behavior. This is articularly true given the crucial importance of the savings ool for financing the deficit and promoting investment and rowth. A forthcoming Treasury study of the taxation of capital ains suggests that lower rates may have produced, at least in he short run, higher receipts. If this is true, should we tax apital gains as we do or consider changes?

We also need to explore the impacts on saving and the use of ax shelters of lowering the top tax rate from 70 percent to 50 ercent, but the full data, unfortunately, will be a year or two in the collection process.

Continuing on taxes, recent studies indicate that workers seem to prefer 60 cents in fringe benefits to a dollar in straight pay. Why is this a mystery, when the average worker is in the 40 percent marginal tax bracket when payroll taxes and Federal, state and local income taxes are taken into account? One doesn't have to be a so-called "supply sider", whatever that is, to understand that the untaxed fringe benefits are worth a lot more than the sixty cents in straight pay left to buy them.

The adverse disincentive effects of high marginal tax rates often appear as refusal to accept overtime work; as pressure for shorter hours, longer vacations and sheltered fringe benefits rather than straight pay increases; as a shift of savings out of ordinary investments into less productive tax shelters or into consumption. Savings incentives and work incentives are both affected.

We make those decisions in Washington. And, all positions will continue to make them with or without a solid economic foundation. You can count on it.

The adverse effects of high and rising marginal tax rates on work incentives are illustrated by paraphrasing President Coolidge's question: "If we had a tax system which took 20 percent of your wages on Monday, 30 percent of your wages on Tuesday, 40 percent of your wages on Wednesday, and so on up to 70 percent of your wages on Saturday, how many days a week would you work?" Well, figuratively speaking, more and more workers are beginning to quit around noon on Thursday.

One can turn Coolidge's question around, and rephrase it in a way that shows its relevance to U.S. employment, labor costs, and the balance of payments. If we had that kind of a tax system, with 50 percent, 60 percent and 70 percent tax rates on Thursday, Friday, and Saturday, what kind of wage or salary would a worker demand from his company before he would consent to work those last three days? Well, we do have it. And thanks to a bipartisan Congressional spending bias, inflation has pushed too many average Americans into those brackets.

Marginal tax rates on wages, interest, and dividends are part of the cost of hiring labor or raising capital. Marginal tax rates, Federal, State and local, are a real cost of doing business in the United States, as opposed to doing business somewhere else. Marginal tax rates are part of the price of U.S. products, as opposed to the price of a product from somewhere else. All other things being equal, don't marginal rate differentials matter? If I'm wrong, please call me collect.

Over the last 15 years, inflation, bracket creep and payroll tax hikes have sharply increased the pre-tax cost to the firm of giving a worker a one dollar after-tax wage increase.

A median income worker now typically faces 40 percent to 44 percent tax rates on added income. (Again, this is the sum of social security and Federal marginal income tax rates, plus state and local taxes at the margin.) It is up sharply from the late 1960s, when the comparable marginal rates would have been roughly 26 percent to 30 percent.

Consequently, it now costs a firm more than $1.70 to compensate a worker for a $1.00 increase in the cost of living. Again, this is up from $1.40 in the late 1960s. Without indexing, it will rise to $2.00 by the late 1980s, and to $2.50 or higher in the 1990s. Any wage increase, whether merely COLA's or a real wage hike, would send taxes rising and tend to push labor costs up faster than the prices the firm receives for its products. Profits, employment, or real wages would tend to fall continutally over time in tne absence of extraordinary productivity increases. The competitive position of U.S. labor in the world economy would suffer. What should our long-run tax reform objective be?

Very few firms can afford to pay their largest factor of ·oduction an increase sharply in excess of the cost of living. :ter all, the cost of living is measured as the rise in the :ices that firms receive for their products. When costs rise ister than prices, the result is reduced profits and declining ıerican productivity in an increasingly interdependent world :onomy.

Bracket creep has tainted labor relations for years and has learly helped to price U.S. labor out of world markets. That tax free" fringe benefit to the worker is a cost that is passed long in international trade. The invisible third party at every argaining table has been the tax collector, using bracket creep ɔ drive a tax wedge deeper and deeper between labor and anagement over time. Marginal rate reduction, followed by ndexing of the exemptions, deductions and tax brackets for nflation starting in 1985, will help prevent this sort of eterioration in the competitive situation of U.S. labor in the uture. Without indexing, the process would merely be arrested or three years by the marginal rate reductions only to resume.

INTERNATIONAL

Let me confess that I am not sure what international conomic policy is. Do you economists have a definition? Let me ave the temerity to suggest a definition. I think that nternational economic policy is the sum of all of the economic olicies that individual countries have when you take into onsideration their affect or impact on other countries, and conomies, or citizens. This may be a somewhat narrower view han many would take, but it appeals to me, because it focuses on he interdependence of the world's economies and does not permit he assumption that there is also domestic economic policy. :ather, it suggests that the bifurcation between international conomic policies and domestic economic policies is an achronism.

Unfortunately, I didn't find this in any of the economic iterature, briefing books, Congressional testimony or learned :reatises in Washington. Rather, like the blind hog with mpaired olfactory senses that still occasionally stumbles across ı truffle, I found it on my own. Is there a body of economic ·esearch that indicates I'm correct? Or, am I wrong?

If this is true, and if we don't know what drives interest ·ates, or whether the Fed should intervene in markets, what can ›ne say about exchange rates? When is the dollar "too strong" or 'too weak"? As judged by what standards? Why is the dollar ·ising while interest rates are falling? Is expected U.S. nflation falling that fast? In fact, I must ask a very basic juestion. Is the dollar "too strong", or are other currencies ;imply "too weak"? We have shown more improvement in inflation :han most of our trading partners. In what sense is this rresponsible or blameworthy?

A charge that has been heard frequently in Washington is that the dollar is over-valued, particularly relative to the yen, because of deliberate intervention. In the presence of a pretty clean float, can anyone claim that the dollar is over- or under-valued? Over- or under-valued against what? The charge has been raised that our high real interest rates are propping up the dollar and choking off exports. Are real interest rates high, or is that a legitimate risk premium on top of a reasonable expected after-inflation interest rate?

I have heard two theories lately on how the Federal deficit affects exchange rates and exports. On the one hand, a high deficit could be said to produce high interest rates and a strong dollar. However, the textbooks say that a high deficit means the government is pushing total national consumption ahead of total national output, with the difference spilling over into imports, which weakens the dollar. Given our projected trade deficit, we would like to know the latest thinking here. One of your most distinguished colleagues, Marty Feldstein, has a view on this. I tend to think he may be correct, but is there a "contrary school"?

There has been a very puzzling development recently. Protectionism seems to be on the rise in the economics profession as well as the Congress. Where do you stand? Is Fortune magazine to be the last and only bastion of free trade?

Some economists have been hinting that substantially increased intervention in international trade may be warranted. They worry about the high cost of adjusting to shifting production patterns when injured industries have been concentrated in particular regions of the country, and when the adjustments have been unusually large and sudden. The popularity of the song "Allentown" is an indication of the depth of feeling. Is it becoming harder to adjust? Are Americans less mobile than they used to be? Did high nominal, but negative real after tax interest rates buy a house for most Americans, but now keep them prisoners in it? Does it become so hard to sell a home in a depressed region that people are unable to move to where the jobs are?

It has always been the hope of the Administration that more predictable fiscal and monetary tax policies, aimed at reducing inflation and increasing economic growth, would spark a period of worldwide investment, productivity gains, improved competitive posture, and solid growth. We felt that the gains worldwide from the growing U.S. economy would help spur trade, and that growth would speed adjustment to new production patterns both here and abroad with a minimum of friction. Unfortunately, recession always maximizes trade friction. Again, given the lags in timing, the political fix of protectionism, spawned by an increasingly immobile labor force, fixes last year's problem -- or maybe the year before that.

We still believe that the gains from free trade outweigh the ain. We need to hear your views on that, and on ways to speed he adjustment process to help our depressed regions. We need our best thinking on these issues.

Last, let me suggest that the leaders of the free world's argest industrial democracies will be coming together in illiamsburg for an economic summit at the end of May. They have hree carry-over items from their meeting in Versailles. They re: the impact of intervention on exchagne rates; the prospects or improving policy convergences on the major countries; and, he impact and transfer of technology. They will be exchanging iews and ideas on these subjects that will influence our own conomy for years to come. Yet, I have the impression there is a osity of literature, research, and analyses on these subjects. et me suggest that these world leaders have provided a judgment, ightly or wrongly, as to what is relevant for economic research. urge you to consider it in framing your own research agendas. lease help us.

CONCLUSION

I've raised a lot of questions here today in my role as a onsumer of economic advice. Indeed, I probably sound like an irate counsumer. I'm not trying to return the merchandise. I'm not asking for a refund. And you can recognize my instinctive skepticism about fine-tuning excesses. I'm certainly not asking for miracles -- such as a method of forecasting turning points in the economy before they happen, or even shortly after they happen. But there are puzzles to be solved which, as a policymaker, I am very concerned about.

What I'm suggesting today is my frustration with economic research and theory. In so doing, I hope I've actually suggested a research agenda for you -- the professionals -- to consider. In my job your work is relevant and important. We make a lot of mistakes in Washington. Future policymakers will also. You can help us minimize these mistakes.

I hope that, in some tranquil and prosperous time ahead, a future Deputy Secretary of the Treasury can look back on the last quarter of this century, and say that, out of the economic upheavals of the period (and the accompanying invaluable flood of data), real advances in economic understanding occurred that made that future of prosperity and stability possible. You can make that happen.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE

March 14, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $ 6,201 million of 13-week bills and for $6,200 million of 26-week bills, both to be issued on March 17, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing June 16, 1983			:	26-week bills maturing September 15, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	97.973	8.019%	8.32%	:	95.837 a/	8.235%	8.74%
Low	97.910	8.268%	8.59%	:	95.817	8.274%	8.78%
Average	97.913	8.256%	8.57%	:	95.822	8.264% 2/	8.77%

a/ Excepting 1 tender of $2,500,000.

Tenders at the low price for the 13-week bills were allotted 16%.
Tenders at the low price for the 26-week bills were allotted 23%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 137,560	$ 45,690	:	$ 162,965	$ 42,215
New York	13,514,325	5,297,685	:	11,637,795	5,031,435
Philadelphia	29,470	27,945	:	18,645	18,645
Cleveland	77,445	44,695	:	111,180	96,180
Richmond	52,840	37,840	:	52,340	30,840
Atlanta	46,685	45,575	:	48,065	36,565
Chicago	1,053,910	168,270	:	828,500	273,300
St. Louis	56,155	44,615	:	70,070	40,070
Minneapolis	15,870	13,370	:	33,850	10,840
Kansas City	46,180	45,055	:	51,595	48,860
Dallas	33,155	28,155	:	17,180	12,180
San Francisco	1,156,695	171,770	:	1,035,380	287,680
Treasury	230,125	230,125	:	271,445	271,435
TOTALS	$16,450,415	$6,200,790	:	$14,339,010	$6,200,245
Type					
Competitive	$14,005,615	$3,755,990	:	$11,770,860	$3,632,095
Noncompetitive	980,570	980,570	:	765,950	765,950
Subtotal, Public	$14,986,185	$4,736,560	:	$12,536,810	$4,398,045
Federal Reserve	1,421,330	1,421,330	:	1,400,000	1,400,000
Foreign Official Institutions	42,900	42,900	:	402,200	402,200
TOTALS	$16,450,415	$6,200,790	:	$14,339,010	$6,200,245

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 8.089%.

R-2081

FOR IMMEDIATE RELEASE MARCH 14, 1983

The Treasury announced today that the 2-1/2 year Treasury yield curve rate for the five business days ending March 14, 1983, averaged 9.70 % rounded to the nearest five basis points. Ceiling rates based on this rate will be in effect from Tuesday, March 15, 1983 through Monday, March 28, 1983.

Detailed rules as to the use of this rate in establishing the ceiling rates for small saver certificates were published in the Federal Register on July 17, 1981.

Small saver ceiling rates and related information is available from the DIDC on a recorded telephone message. The phone number is (202)566-3734.

Approved ______________________
Francis X. Cavanaugh, Director
Office of Government Finance
& Market Analysis

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE ON DELIVERY
March 15, 1983 - 11:30 A.M.

STATEMENT OF THE HONORABLE JOHN M. WALKER, JR.
ASSISTANT SECRETARY (ENFORCEMENT & OPERATIONS)
U.S. DEPARTMENT OF THE TREASURY
BEFORE THE
PERMANENT SUBCOMMITTEE ON INVESTIGATIONS
OF THE
COMMITTEE ON GOVERNMENTAL AFFAIRS
UNITED STATES SENATE

Transnational Investigations and the Bank Secrecy Act

Mr. Chairman and Members of the Subcommittee:

Thank you for the opportunity to present our views on the problems raised by the use of foreign corporations and financial institutions to facilitate violations of U.S. law. Our interest in this subject flows naturally from the interests and functions of two Treasury law enforcement agencies, IRS and Customs, to protect the revenue and our national economic interests, as well as to collect taxes and duties. In addition, since the passage of the Bank Secrecy Act in 1970, we have had a special responsibility with respect to transnational investigations.

When the Bank Secrecy Act was introduced by the Chairmen of the Senate and House Banking Committees, it was clear that they intended the Bank Secrecy Act to play a major role in combatting the use of foreign bank accounts to facilitate violations of U.S. laws. During the hearings that preceded the passage of the Bank Secrecy Act, officials from several government agencies testified concerning the need for assistance in identifying suspicious transactions and movements of currency and documenting international transactions in general. The Act was intended to assist law enforcement officials by providing for the retention of records of all significant international transactions as well as reports of unusual domestic currency transactions, the international transportation of currency and other monetary instruments, and reports of international financial transactions or accounts. It is the linchpin for all investigations of financial activity; it was specifically designed to deter transnational crimes.

The reporting requirements of the Bank Secrecy Act provide a unique way to follow unusual cash flows including cash flows caused by major drug traffickers and their money launderers. Indeed, the tracking of cash flows through the reporting requirements of the Act frequently leads to the identification of drug trafficking organizations. As an added bonus, the Bank Secrecy Act imposes criminal sanctions on those who fail to comply with its requirements. The major narcotics trafficker, who carefully insulates himself from actually handling drugs, can still be brought before the bar of justice for failure to comply with the reporting requirements of the Bank Secrecy Act or for income tax violations, even though there may be an inability to establish the underlying narcotics offense.

The Act authorizes the Secretary of the Treasury to issue regulations to carry out the purposes of the Act. The principal provisions are:

1. Banks and other financial institutions must maintain records that the Secretary determines have a high degree of usefulness in criminal, tax, or regulatory investigations.

2. They must report to the Treasury Department transactions involving currency or other monetary instruments as the Secretary may require.

3. The international transportation of currency and other monetary instruments in excess of $5,000 must be reported to the Treasury Department.

4. The Secretary must require U.S. citizens, residents, and persons doing business in the United States to maintain records or file reports, or both, of foreign financial transactions.

<u>Regulations</u>

After considering the Congressional mandate expressed in the Act and the committee reports, the Treasury Department issued regulations which currently contain the following recordkeeping requirements:

1. All financial institutions are required to maintain the following records:

   a. Instructions, given or received, concerning the transmission out of the U.S. of credit funds, currency or other monetary instruments, checks or securities of more than $10,000.

   b. Each extension of credit in excess of $5,000 except for those secured by real estate.

2. Banks, savings and loans, and credit unions must also retain a copy of the following records:

   a. Documents granting signature authority over each deposit or share account.

   b. Statements of accounts.

   c. Checks and other charges in excess of $100 that are posted to accounts. (Checks drawn on certain volume accounts are exempted.)

   d. Each check or other item in excess of $10,000 transmitted outside the U.S.

   e. Each check or draft in excess of $10,000 drawn on or issued by a foreign bank which is paid by the domestic bank.

   f. Each check in excess of $10,000 received directly from a foreign financial institution.

   g. Records of each receipt of currency, other monetary instrument, securities, checks or credit received from a foreign financial institution.

h. Records necessary to reconstruct a checking account and to furnish an audit trail for each account transaction over $100.

3. Securities brokers under the supervision of the SEC have been subject to recordkeeping regulations for many years. The Treasury regulations, however, added the requirement that brokers obtain a signature card or similar document establishing trading authority over an account and make a reasonable effort to obtain a Social Security number of each account.

In addition, the regulations prescribed the following reporting requirements:

1. Financial institutions are required to report to the IRS domestic currency transactions in excess of $10,000 (IRS Form 4789). Transactions with retail type businesses and other domestic banks are exempted.

2. Except for certain shipments made by banks, the international transportation of currency and certain other monetary instruments in excess of $5,000 are required to be reported to the Customs Service (Customs Form 4790).

3. U.S. persons are required to report annually a financial interest in or signature authority over a foreign financial account. Certain records of such an account are required to be maintained in the U.S.

Compliance Responsibilities

Sections 128 and 205 of the Act, which gave the Secretary the responsibility for assuring compliance, also gave him authority to delegate such responsibility to the appropriate bank supervisory agency or other supervisory agency.

In accordance with that authority, the responsibility for assuring compliance with the requirements of the regulations has been delegated as follows:

1. To the Comptroller of the Currency, with respect to national banks and banks in the District of Columbia;

2. To the Board of Governors of the Federal Reserve System, with respect to State bank members of the Federal Reserve System;

3. To the Federal Home Loan Bank Board, with respect to insured building and loan associations, and insured institutions as defined in section 401 of the National Housing Act;

4. To the Administrator of the National Credit Union Administration, with respect to Federal credit unions;

5. To the Federal Deposit Insurance Corporation, with respect to all other banks except agents of foreign banks which agents are not supervised by State or Federal bank supervisory authorities;

6. To the Securities and Exchange Commission, with respect to brokers and dealers in securities;

7. To the Commissioner of Customs with respect to reports of transportation of currency or monetary instruments and forfeiture of currency or monetary instruments;

8. To the Commissioner of Internal Revenue except as otherwise specified. This means, in effect, that the IRS has the responsibility for enforcement of those sections requiring persons who have foreign bank accounts to report them and to keep records pertaining to them, and those sections requiring financial institutions to report large and unusual currency transactions, as well as a responsibility to make certain that dealers in foreign exchange, transmitters of funds, unsupervised or secret agents of foreign banks, and similar financial institutions are complying with the recordkeeping provisions of the regulations.

Overall responsibility for coordinating the procedures and efforts of the agencies listed above and for assuring compliance with the regulations has been delegated to my office.

The regulations were designed to provide an integrated system for tracing and documenting the overwhelming majority of financial transactions that might be of interest to investigators. Financial institutions are required to maintain records of checks, wire transfers, and other movements of funds and be able to reconstruct transactions accounts. The currency transaction reports and reports of the international movement of monetary instruments are intended to fill the gaps in the system resulting from the use of currency and bearer instruments. In addition, the reports are also intended to alert the law enforcement community to specific activity that appears to warrant investigation.

We recognize that we are very dependent on the Federal bank supervisory agencies. Their bank examiners have the primary responsibility for the enforcement of the regulations. The examiners must see that the records are retained and the unusual currency transactions are properly reported. In recent years, they have made a major commitment to the enforcement of the Bank Secrecy Act. In 1981, they began using expanded examination procedures which require them to review retained copies of currency transaction reports and to ascertain that a financial institution has a program of employee education, written operating procedures, and an adequate internal compliance program.

FLEC

In 1982, the Financial Law Enforcement Center (FLEC) was established within Customs. The Center has assumed the responsibility for collecting, collating, and analyzing the report data obtained from the three reports required to be filed with the Treasury Department under the provisions of the Bank Secrecy Act. These functions were performed previously by the Reports Analysis Unit which was superseded by FLEC. FLEC assists law enforcement agencies in developing strategies that will exploit the vulnerability of the financial aspects of criminal activity. FLEC combines the talents of criminal investigators intelligence research analysts, and ADP specialists into one integrated organization. At the present time, both Customs and IRS have assigned employees to FLEC.

Administrative Actions

In 1980, we realized from our review of compliance in Florida that the regulations pertaining to the currency transaction reports needed to be tightened up. Some banks had been exempting individuals with Latin American addresses from the currency transaction reporting requirements because these persons brought large amounts of currency into the bank on a regular basis. Unfortunately, too often these customers also happened to be suspected drug traffickers. In addition, some banks frequently accepted shopping bags or boxes of currency from couriers whose identity they did not bother to verify.

The regulations were amended in 1980 to limit a bank's authority to exempt currency transactions from the reporting requirements. Only deposits and withdrawals by an established depositor, who is a U.S. resident and operates a retail business in the U.S. can be exempted without the approval of the Treasury Department. More specific identification requirements were also provided. Financial institutions are now required to verify the identity of persons who conduct reportable currency transactions with them. The identity of aliens and persons who are not U.S. residents must be made by passport, or some other official document. While these changes have created an additional burden for banks, there is no doubt in my mind that they were justified.

We have taken several other actions to improve filing compliance and the quality of the currency transaction report data base:

1. The IRS corresponds on reports which do not meet the minimum criteria for processing and, if they are unable to resolve the problem through correspondence, the report is referred to the responsible supervisory agency.

2. The IRS is revising Publication 1148 in order to provide more detailed instructions for the preparation of the currency transaction report.

3. Guidelines for the compliance agencies to use in recommending civil penalties for violations of the regulations are now in the final review process.

4. The Florida State Banking Division has been very active in checking state chartered banks for compliance with the reporting provisions. We have been assisting them in that effort and have been exploring other ways in which they could help with the money laundering problem in Florida.

5. We have been developing summary reports of the report data for use by the bank supervisory agencies in checking compliance with the currency transaction reporting requirements and in identifying areas of the nation where compliance appears to be low.

Obviously, as the quality of the data base improves, the the more useful it will become, not only for individual investigations but for analytical reports. For example, we have found that analysis of the volume of currency transactions between U.S. banks and foreign persons or institutions is very valuable in indicating areas where additional investigative action should be taken.

Operation Greenback

In 1980, Treasury's Office of Enforcement and Operations, with the cooperation of the IRS, Customs, and the Department of Justice, developed Operation Greenback. It is an integrated investigation of the huge surplus of currency in the Federal Reserve banks in Florida which we believe results, in part, from illegal activity. The surplus grew from $1.5 billion in 1976 to a peak of $5.8 billion in 1980. In 1982 it declined to $5.3 billion. Operation Greenback was based primarily on two concepts. First, an attack on the illegal activity associated with the currency could be made through the financial operations of the violators. The tax laws and the reporting and recordkeeping requirements of the Bank Secrecy Act, could be effectively employed in this effort. Second, the criminal investigations should be integrated through the use of the grand jury process with Federal prosecutors coordinating all of the related investigations. Since the inquiry is being conducted under the authority of a grand jury, all of the Federal agents participating in it can pool information, including tax or other financial information. This kind of sharing which streamlines the investigative process, is not permitted under the procedures governing administrative inquiries.

The Operation Greenback strategy also included certain administrative actions. Through the analysis of Federal Reserve bank records, currency transaction reports, and related information, Treasury identified 24 banks that had handled unusually large amounts of currency. Those banks were given special indepth examinations by the Federal banking authorities. The examinations identified several institutions where investigations of possible criminal violations were initiated. The IRS was also encouraged to undertake civil tax examinations of those persons involved in unusual, large currency transactions.

Operation Greenback has documented $2,065,000,000 in U.S. currency that has been laundered through international transactions by seven different organizations. The amounts for each are listed below. The schedule does not necessarily include all of the currency laundered by each organization, nor the entire length of time it was in operation.

Case Designation	U.S. Currency Laundered	Time Frame
A	$ 300,000,000	2 Years
B	500,000,000	3 Years
C	268,000,000	5 Months
D	250,000,000	20 Months
E	130,000,000	3 Years
F	300,000,000	3 Years
G	70,000,000	8 Months
H	17,000,000	8 Months
I	230,000,000	3 Years
Total	$2,065,000,000	

The above figures are from cases either under investigation, indicted or prosecuted.

During the 30 months of operation, ending December 31, 1982, Treasury has seized more than $28 million in currency. In addition, property in excess of $2.5 million has been seized. Appearance bonds in excess of $1.8 million have been forfeited and jeopardy tax assessments totalling more than $112 million have been made. There are approximately 40 special agents from IRS and Customs assigned to Operation Greenback.

The combined effort of the IRS and U.S. Customs Service has resulted in approximately 140 indictments, 44 convictions, and approximately 90 cases are pending trial.

Other Significant Cases

Although Operation Greenback cases tend to overshadow the other cases, a large number of significant Bank Secrecy Act investigations are underway in many cities across the country. (More than 20 financial investigative task forces have been established throughout the United States and Puerto Rico.) Several of the investigations involve international transactions or foreign financial institutions. For example, a Federal strike force investigation initiated by Customs in Detroit resulted in the conviction, in 1981, of a group of individuals who were charged with a criminal conspiracy to launder money in order to convert corporate assets to their own use, bribe employees of commercial customers, and evade taxes. The scheme involved the transportation of monetary instruments to Canada, where they were converted to cashiers checks. Civil penalties under the Bank Secrecy Act of about $1,000,000 were also assessed in this case.

In another case in October, 1981, a bank in California and its chairman pled guilty to Bank Secrecy Act charges that involved drugs, tax evasion, and international financial transactions. The bank official and other defendants were charged with conspiring with an attorney to provide money laundering services for narcotics traffickers who had large quantities of currency that were derived from their illegal activities. The currency was accepted by the bank and the funds were wired to trusts at the Bank of Bermuda. The funds were then wired back to the United States for the traffickers. The attorney prepared fictitious documents to make it appear that the money from the trusts had a legitimate non-taxable source.

Need to Amend the Bank Secrecy Act and Regulations

Mr. Chairman, as I have recited in this statement, a massive effort has been made to ensure that the records needed to trace financial transactions through banks in this country are available for law enforcement purposes. To the best of my knowledge, that effort has been very successful. Transactions that occur in this country can be documented. In addition, Customs, IRS and other Federal supervisory agencies are expending a great amount of time in obtaining compliance with the reporting requirements and in analyzing the report data. However, in spite of our successes there is abundant evidence that much more needs to be done. Information available to us indicates that millions of dollars in cash is being transported out of the country without filing the required currency and monetary investments report. Foreign banks and corporations continue to be used to thwart our efforts to enforce the law. In my opinion, much of the weakness in the system could be overcome by making the following changes in the Bank Secrecy Act:

1. Amend Section 5316 of Title 31 by making it a crime to "attempt to transport or cause to be transported" monetary instruments in excess of $10,000 without filing a report with Treasury (Customs).

2. Amend Section 5317 of Title 31 by authorizing Customs officers to stop and search a vehicle, vessel, aircraft or other conveyance, envelope or other container, or person entering or departing the United States if there is reasonable cause to believe there is a violation of the reporting requirements.

3. Add a new section authorizing the Secretary of the Treasury to pay rewards, except to certain Federal, State and local officers, for original information leading to the recovery of a fine, penalty, or forfeiture exceeding $50,000. It should provide that the Secretary shall determine the amount of the reward but in no case shall it exceed 25 percent of the net amount of the fine, penalty, or forfeiture assessed. There should also be a provision for necessary appropriations.

However, I believe that the information that we have received from the investigative efforts in Florida and the analysis of financial data indicate that we also need to take action to strengthen our Treasury regulations. We are going to draft amendments to the Bank Secrecy Act regulations that would require currency exchanges and the dealers in foreign exchange to maintain adequate records of their transactions. These institutions have played a major role in laundering money in Florida and other states. They function like a bank in many respects and should be subject to the same type of recordkeeping provision as banks.

In addition, it appears that the time has come to more fully utilize the Treasury Department's authority to require reports of foreign financial transactions. There have been many statements regarding the need for law enforcement agencies to be alerted to unusual international movement of funds by cashiers check, wire transfer, or other methods. Although the Bank Secrecy Act (31 U.S.C. 5314) would authorize a requirement that such transactions be reported to the Treasury Department, we have been reluctant to exercise it. There are too many international transactions that are related to legitimate commerce to warrant a shotgun solution to the problem. Nevertheless, it is increasingly clear that law enforcement officials need assistance in identifying those persons who are using foreign financial facilities to further their criminal activities. In my opinion, a reasonable approach to the problem would be for the Treasury Department, on the basis of information indicating that there has been a probable misuse of foreign financial facilities by U.S. persons, to impose selective reporting. For example, if there is reason to believe that banks in a foreign country are being utilized to further illegal activity, the Secretary could require specific classes of persons or domestic financial institutions to report their transactions with these foreign banks. We believe that such a requirement would be extremely useful to the IRS in tax enforcement, as well as to other Federal agencies interested in transnational crime.

Banks located in offshore tax havens are ideally suited to the purposes of the narcotics trafficker. We have seen in Operation Greenback a number of situations where U.S. currency has been laundered through international transactions. The trafficker's goal, once he has sold his product, is to hide his money or to cleanse his money so that he can put it to use without it being attributed to him as unreported income. A tax haven with bank secrecy facilitates achievement of this goal by providing a veil of secrecy over parts of the transaction, so that the taxpayer cannot be definitely tied to the flow of funds. Furthermore, the tax haven's infrastructure, which often includes modern banking and communications facilities, serves to facilitate rapid movement of funds.

The problem can be illustrated by a simple case. A narcotics trafficker arranges for a courier to carry $200,000 in cash in a suitcase to the Cayman Islands where it is deposited in a small so-called "offshore bank". The courier does not file a Form 4790. The money goes into an account of a Bahamian registered company which is purchased for a small sum. Business transactions are then run through this company. The company then transfers $100,000 to an account in its name at the branch of a large money center bank. The narcotics trafficker then borrows $100,000 from the Bahamian company. Both the trafficker and the corporation claim that the loan is simply a signature loan to an individual. In fact, the loan is effectively secured by the Cayman deposit.

Similarly, the drug trafficker can get funds to an offshore bank by having a courier open an account in a Miami bank in a fictitious name and deposit large sums of cash in a short period of time. The money in the deposit can then be wired to an offshore bank and handled in the same manner as outlined above. The courier presumably "beats the system" by using a fictitious identification in an effort to avoid detection.

Amendments to the Bank Secrecy Act which would give the Customs Service an attempt provision and an outbound search authority would help in our efforts to get the courier who transports large sums of cash to offshore banking havens without filing the requisite form. The existing provisions of the Bank Secrecy Act help us to identify and prosecute the courier who makes large cash deposits in a domestic bank. The regulatory changes which we are considering would require specific domestic financial institutions to report their transactions with banks in certain foreign countries. This would assist us in overcoming the advantages of using offshore banking havens to shield questionable transactions from government scrutiny.

Mr. Chairman, I would appreciate it if the Subcommittee would consider and support these proposals. I believe that they would be major contributions to our efforts to overcome the use of foreign banks to conceal illegal activity.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-204

FOR RELEASE AT 4:00 P.M. March 15, 1983

TREASURY'S WEEKLY BILL OFFERING

The Department of the Treasury, by this public notice, invites tenders for two series of Treasury bills totaling approximately $12,400 million, to be issued March 24, 1983. This offering will provide $ 900 million of new cash for the Treasury, as the maturing bills were originally issued in the amount of $11,496 million. The two series offered are as follows:

91-day bills (to maturity date) for approximately $ 6,200 million, representing an additional amount of bills dated December 23, 1982, and to mature June 23, 1983 (CUSIP No. 912794 CY 8), currently outstanding in the amount of $ 5,811 million, the additional and original bills to be freely interchangeable.

182-day bills for approximately $ 6,200 million, to be dated March 24, 1983, and to mature September 22, 1983 (CUSIP No. 912794 DR 2).

Both series of bills will be issued for cash and in exchange for Treasury bills maturing March 24, 1983. In addition to the maturing 13-week and 26-week bills, there are $5,277 million of maturing 52-week bills. The disposition of this latter amount was announced last week. Federal Reserve Banks, as agents for foreign and international monetary authorities, currently hold $ 1,817 million, and Federal Reserve Banks for their own account hold $ 3,967 million of the maturing bills. These amounts represent the combined holdings of such accounts for the three issues of maturing bills.

Tenders from Federal Reserve Banks for themselves and as agents for foreign and international monetary authorities will be accepted at the weighted average prices of accepted competitive tenders. Additional amounts of the bills may be issued to Federal Reserve Banks, as agents for foreign and international monetary authorities, to the extent that the aggregate amount of tenders for such accounts exceeds the aggregate amount of maturing bills held by them. For purposes of determining such additional amounts, foreign and international monetary authorities are considered to hold $ 1,312 million of the original 13-week and 26-week issues.

The bills will be issued on a discount basis under competitive and noncompetitive bidding, and at maturity their par amount will be payable without interest. Both series of bills will be issued entirely in book-entry form in a minimum amount of $10,000 and in any higher $5,000 multiple, on the records either of the Federal Reserve Banks and Branches, or of the Department of the Treasury.

Tenders will be received at Federal Reserve Banks and Branches and at the Bureau of the Public Debt, Washington, D. C. 20226, up to 1:30 p.m., Eastern Standard time, Monday, March 21, 1983. Form PD 4632-2 (for 26-week series) or Form PD 4632-3 (for 13-week series) should be used to submit tenders for bills to be maintained on the book-entry records of the Department of the Treasury.

Each tender must be for a minimum of $10,000. Tenders over $10,000 must be in multiples of $5,000. In the case of competitive tenders the price offered must be expressed on the basis of 100, with three decimals, e.g., 97.920. Fractions may not be used.

Banking institutions and dealers who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities may submit tenders for account of customers, if the names of the customers and the amount for each customer are furnished. Others are only permitted to submit tenders for their own account. Each tender must state the amount of any net long position in the bills being offered if such position is in excess of $200 million. This information should reflect positions held as of 12:30 p.m. Eastern time on the day of the auction. Such positions would include bills acquired through "when issued" trading, and futures and forward transactions as well as holdings of outstanding bills with the same maturity date as the new offering, e.g., bills with three months to maturity previously offered as six-month bills. Dealers, who make primary markets in Government securities and report daily to the Federal Reserve Bank of New York their positions in and borrowings on such securities, when submitting tenders for customers, must submit a separate tender for each customer whose net long position in the bill being offered exceeds $200 million.

Payment for the full par amount of the bills applied for must accompany all tenders submitted for bills to be maintained on the book-entry records of the Department of the Treasury. A cash adjustment will be made on all accepted tenders for the difference between the par payment submitted and the actual issue price as determined in the auction.

No deposit need accompany tenders from incorporated banks and trust companies and from responsible and recognized dealers in investment securities for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches. A deposit of 2 percent of the par amount of the bills applied for must accompany tenders for such bills from others, unless an express guaranty of payment by an incorporated bank or trust company accompanies the tenders.

Public announcement will be made by the Department of the Treasury of the amount and price range of accepted bids. Competitive bidders will be advised of the acceptance or rejection of their tenders. The Secretary of the Treasury expressly reserves the right to accept or reject any or all tenders, in whole or in part, and the Secretary's action shall be final. Subject to these reservations, noncompetitive tenders for each issue for $500,000 or less without stated price from any one bidder will be accepted in full at the weighted average price (in three decimals) of accepted competitive bids for the respective issues.

Settlement for accepted tenders for bills to be maintained on the book-entry records of Federal Reserve Banks and Branches must be made or completed at the Federal Reserve Bank or Branch on March 24, 1983, in cash or other immediately-available funds or in Treasury bills maturing March 24, 1983. Cash adjustments will be made for differences between the par value of the maturing bills accepted in exchange and the issue price of the new bills.

Under Section 454(b) of the Internal Revenue Code, the amount of discount at which these bills are sold is considered to accrue when the bills are sold, redeemed, or otherwise disposed of. Section 1232(a)(4) provides that any gain on the sale or redemption of these bills that does not exceed the ratable share of the acquisition discount must be included in the Federal income tax return of the owner as ordinary income. The acquisition discount is the excess of the stated redemption price over the taxpayer's basis (cost) for the bill. The ratable share of this discount is determined by multiplying such discount by a fraction, the numerator of which is the number of days the taxpayer held the bill and the denominator of which is the number of days from the day following the taxpayer's date of purchase to the maturity of the bill. If the gain on the sale of a bill exceeds the taxpayer's ratable portion of the acquisition discount, the excess gain is treated as short-term capital gain.

Department of the Treasury Circulars, Public Debt Series - Nos. 26-76 and 27-76, and this notice, prescribe the terms of these Treasury bills and govern the conditions of their issue. Copies of the circulars and tender forms may be obtained from any Federal Reserve Bank or Branch, or from the Bureau of the Public Debt.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. March 15, 1983

TREASURY BILL AUCTIONS TO USE NEW BIDDING METHOD
EFFECTIVE APRIL 18, 1983

The Treasury announced today that a new method of competitive bidding for Treasury bills will be required effective with the regular weekly auctions scheduled for Monday, April 18, 1983.

For the first time in Treasury bill auctions, bidding will be on a bank discount yield basis rather than on a price basis. Competitive bidders will be required to state the percentage yield (on a bank discount basis) that they will accept to two decimal places, for example, 7.89 percent. The calculation of purchase prices for accepted bids will be carried to three decimal places on the basis of price per hundred, e.g., 99.923, and each successful competitive bidder will pay the price equivalent to his bid. Noncompetitive bidders will pay the price equivalent to the weighted average discount yield in the particular auction.

The change in method will conform the bidding in Treasury bill auctions to market pricing conventions and simplify the submission of tenders.

The details and conditions of the first offering of bills using the new bidding method will be separately announced in the normal course on Tuesday, April 12, 1983.

R-2084

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE AT 4:00 P.M. March 15, 1983

TREASURY ANNOUNCES NOTE AND BOND OFFERINGS TOTALING $13,500 MILLION

The Treasury will raise about $10,600 million of new cash by issuing $5,500 million of 4-year notes, $4,750 million of 7-year notes, and $3,250 million of 20-year 1-month bonds. This offering will also refund $2,918 million of 4-year 1-month notes maturing March 31, 1983. The $2,918 million of maturing 4-year 1-month notes are those held by the public, including $320 million currently held by Federal Reserve Banks as agents for foreign and international monetary authorities.

The $13,500 million is being offered to the public, and any amounts tendered by Federal Reserve Banks as agents for foreign and international monetary authorities (including $1,522 million of maturing 2-year and 4-year 1-month notes) will be added to that amount.

In addition to the public holdings, Government accounts and Federal Reserve Banks, for their own accounts, hold $900 million of notes (including the $888 million of 2-year notes previously announced) that may be refunded by issuing additional amounts of the new 2-year and 4-year notes at the average prices of accepted competitive tenders.

Details about each of the new securities are given in the attached "highlights" of the offerings and in the official offering circulars.

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Attachment

R-2085

HIGHLIGHTS OF TREASURY OFFERINGS TO THE PUBLIC
OF 4-YEAR NOTES, 7-YEAR NOTES, AND 20-YEAR 1-MONTH BONDS

March 15, 1983

Amount Offered:			
To the public	$5,500 million	$4,750 million	$3,250 million
Description of Security:			
Term and type of security	4-year notes	7-year notes	20-year 1-month bonds
Series and CUSIP designation	Series H-1987 (CUSIP No. 912827 PH 9)	Series D-1990 (CUSIP No. 912827 PJ 5)	Bonds of 2003 (CUSIP No. 912810 DD 7)
Issue date	March 31, 1983	April 4, 1983	April 4, 1983
Maturity date	March 31, 1987	April 15, 1990	May 15, 2003
Call date	No provision	No provision	No provision
Interest rate	To be determined based on the average of accepted bids	To be determined based on the average of accepted bids	To be determined based on the average of accepted bids
Investment yield	To be determined at auction	To be determined at auction	To be determined at auction
Premium or discount	To be determined after auction	To be determined after auction	To be determined after auction
Interest payment dates	September 30 and March 31	October 15 and April 15 (first payment on October 15, 1983)	November 15 and May 15 (first payment on November 15, 1983)
Minimum denomination available	$1,000	$1,000	$1,000
Terms of Sale:			
Method of sale	Yield Auction	Yield Auction	Yield Auction
Competitive tenders	Must be expressed as an annual yield, with two decimals, e.g., 7.10%	Must be expressed as an annual yield, with two decimals, e.g., 7.10%	Must be expressed as an annual yield, with two decimals, e.g., 7.10%
Noncompetitive tenders	Accepted in full at the average price up to $1,000,000	Accepted in full at the average price up to $1,000,000	Accepted in full at the average price up to $1,000,000
Accrued interest payable by investor	None	None	None
Payment by non-institutional investors	Full payment to be submitted with tender	Full payment to be submitted with tender	Full payment to be submitted with tender
Deposit guarantee by designated institutions	Acceptable	Acceptable	Acceptable
Key Dates:			
Deadline for receipt of tenders	Tuesday, March 22, 1983, by 1:30 p.m., EST	Wednesday, March 23, 1983, by 1:30 p.m., EST	Thursday, March 24, 1983, by 1:30 p.m., EST
Settlement date (final payment due from institutions)			
a) cash or Federal funds	Thursday, March 31, 1983	Monday, April 4, 1983	Monday, April 4, 1983
b) readily collectible check	Tuesday, March 29, 1983	Thursday, March 31, 1983	Thursday, March 31, 1983

Telephone Message for Small Saver Certificate Rates

The DIDC has determined that the small saver certificate ceiling rates based on the Treasury's 2-1/2-year yield curve rate will be 9.70 % for thrift institutions and 9.45 % for commercial banks for the period March 15, 1983 through March 28, 1983.

The next 2-1/2 year rate announcement will be March 28, 1983 at approximately 5:30 p.m. Eastern time..

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE UPON DELIVERY
Wednesday, March 16, 1983

SECRETARY OF THE TREASURY
DONALD T. REGAN
BEFORE THE ECONOMIC CLUB OF DETROIT
WEDNESDAY, MARCH 16, 1983

From Recovery to Renewal

It's conventional for a speaker to open his remarks with some humorous story designed to disarm his critics and seduce his audience -- a sort of literary shot across the bow, reflecting well upon both firer and target. I don't want to be quite so conventional this afternoon. Not in a city that has witnessed as much pain as Detroit. Not among people who have sacrificed so willingly. Not within earshot of families who have struggled to make ends meet, and sometimes questioned whether their country would ever renew her long lease on prosperity.

Perhaps you've noticed by now that the President for whom I work isn't afraid of being unconventional either. When he took office a little more than two years ago, conventional wisdom had it that no chief executive could surmount political tradition and a locust cloud of special interests to wage an effective war against inflation. No one man, it was said, could make good on his promises to reduce taxes, reform the spider's web of excessive regulations, curb the voracious hunger of Washington's big spenders, and reverse the misguided economic policies that dulled American competitiveness and drained off billions of dollars from productive investment and job creation.

But I invite you to consider the latest numbers disgorged by capital computers. Two years ago, consumer prices were rising at an annual rate of better than 12%. Today, the CPI stands at 3.9%. And with oil prices continuing to slide, virtually no one seriously expects any re-ignition of the inflationary fires anytime soon. Two years ago, interest rates were topping out at 21 1/2%. Today, they're less than half that figure, and the rewards for patience can be counted in every real estate office in America, not to mention a great many auto showrooms, lumber mills, and brokerage houses. Two years ago, the federal budget was growing at a yearly clip of 14% -- and my use of the word clip is not accidental. Today, Uncle Sam is tightening his belt just as millions of those who support him with their taxes have had to do. Those taxpayers will receive a windfall of $335 billion or so between now and 1985 -- money they never would have seen, let alone spent, were it not for the economic reform program adopted at the President's urging in 1981.

None of this fits the conventional mold as sculpted by pre-Reagan Washington. Nor have the rites of passage been

R-2086

navigated painlessly. Thanks to the skyhigh interest rates we inherited, we found ourselves in a recession far deeper and far more prolonged than anyone expected. But as the tax cut medicine prescribed in the spring of 1981 has taken hold, as savings have swelled and consumer spending expanded, as the perception of reduced inflation rose up to meet the reality, as investors came to accept our long-range commitment to fight inflation with more than words -- well, the unconventional is in the process of vindication.

In addition to the impressive progress against inflation and interest rates, we can now measure month by month the rebound of an economy primed for significant growth and sustained prosperity. "An optimist," Winston Churchill liked to say, "sees an opportunity in every calamity, a pessimist sees a calamity in every opportunity." In case you haven't guessed by now, I'm an optimist. And even in Washington, that outpost of tunnel vision, it's hard to miss the opportunities as omnipresent as press releases and cameramen.

The recession is over, by virtually any statistical measurement at hand. January's increase in the leading economic indicators was 3.6% -- the largest spurt since Harry Truman occupied the White House in July, 1950. Industrial production has risen over the last three months. Factory utilization has halted its decline, and durable goods orders have posted three straight months of solid gains. Housing starts have reached their highest levels in years. Auto sales, although still well below the golden age of the mid-70's, are nonetheless rebounding from last year's pace. Inventories continued to fall in January, on the heels of the sharpest liquidation since World War II.

Most important of all, the unemployment rate has peaked at 10.8% and retreated to 10.4. That is still too high -- far too high for any of us to claim ultimate victory in the economic battle still being waged. But on top of so much persuasive evidence that the worst is behind us, and with the knowledge that employment usually trails behind other indexes of economic performance by several months, it's fair to say that the American economy is not only poised for recovery -- it has already begun to generate fresh opportunity.

According to the National Association of Purchasing Management, incoming orders are rising steadily, and the employment picture is brighter than at any time in more than a year. Just ten weeks ago, these same purchasing chiefs were asked to give their assessment of the first quarter of 1983. Twenty-eight percent predicted improvement over the same period last year; 15% forecast a worse quarter. But according to the latest survey, 58% of the purchasing managers replied that this quarter would show improvement over last year. The ranks of the pessimists had dwindled to just 11%.

If only the same ratio held true for Congress and the media.

None of this is said in the spirit of self-congratulation. As long as auto workers in Detroit go without paychecks; as long as men and women who want to spend their days on the assembly line are condemed instead to the unemployment line; as long as inner city kids are confined to streetcorners without hope and neighborhoods without prospects for outside investment; as long as the promise of free enterprise, which is colorblind and universal, fails to include any of our citizens; then none of us can afford to relax in what is at heart a struggle for social justice as well as jobs. The entire Reagan Revolution, so-called, is based on the idea that less government and more capitalism might at last attack at their roots the overgrowth of crushed dreams and blasted opportunities that have mocked our claims to compassion and wasted our most precious asset, which is people.

We ought not forget this as we begin to move from recession to recovery. How can we avoid the tragic experiences of the recent past, when two short-lived booms were snuffed out before they got beyond the stage of infancy? How can we raise the floor beneath those now in distress, without lowering the ceiling on future growth and future emloyment?

It's been said that it is the business of the future to be dangerous. I couldn't disagree more strongly. I look beyond the headlines to see the horizon, and I see an economy of enormous untapped potential. Not just in computer chips and not just in the high tech belts of Route 128 and the Silicon Valley. But on assembly lines and in industrial plants, in Detroit and Pittsburgh, wherever men and women with imagination as well as capital decide to exploit the one while investing the other.

First things first. Millions of our people still hurt. They deserve more than pious words and congressional hearings. To address the problems of structural unemployment, the President is proposing a number of steps. One is a voucher system, permitting workers to swap unemployment benefits for job vouchers, which would, in turn, entitle employers to tax credits. In addition, he has called for a thousand per cent increase in funds targeted to displaced workers under the Job Training Partnership Act. More money than ever before would reach the states to permit job retraining, placement and relocation assistance. In place of CETA, which even its friends acknowledge was flawed by administrative overhead and insufficient attention to long-term employment, the administration is seeking three billion dollars to train workers for jobs that will outlast a government program, and paychecks that do not depend upon the whim of a congressional committee.

For young people who suffer a disproportionate share of unemployment, we propose to open the door to opportunity -- without shutting it in the face of adult workers. During the summer months, we would permit employers to hire teenagers at \$2.50 per hour. We would not permit anyone to be hired at the expense of current workers -- and if you doubt my word on that, I'll refer you to a stiff set of penalties, including heavy fines or a year in jail. No solution is perfect, but compared with the nightmare of teenage unemployment -- up to 45% among black teenagers in Detroit and similar cities -- we can no longer stand by and allow the status quo to serve as an excuse for inaction.

In addition to these steps, the President has signalled his unwavering opposition to those who would scrap either the third year of his across the board tax cut, or tax indexing, now scheduled to take effect in 1984. Let's be honest, with ourselves and with our children. The tax cuts adopted in 1981 did little more than keep our heads above water. They did call a halt to the rapidly increasing trends evident in the late 70's, and they put us more nearly on an equal footing with tax levels applied in the more prosperous 60's. Those with a fondness for yesterday's policies cloak their nostalgia in the seductive language of fairness. Of course, they never tell us what was fair about double-digit inflation, record interest rates, or the decline in purchasing power fostered by their own inclination to spend now and send the bill to future generations. It's as if we'd created a new beatitude: "Blessed are the young, for they shall inherit the national debt."

The facts, of course, are simple. Those who earn between $10,000 and $60,000 a year -- what is generally defined as the broad middle class of Americans -- pay about three-quarters of all income taxes. They receive about three-quarters of the income tax cut. But in adition to that, they receive a disproportionate boost in the value of their dollars when you figure in a dramatically reduced inflation rate. To repeal the third year of the tax cut now would impose comparatively little hardship on the wealthy. For those with incomes of $200,000 or more, it would mean a tax hike of less than 3%. But for those whose adjusted gross income is less than $10,000 a year, repeal of this July's tax cut would impose nearly 14% of additional tax liability. For those in the twenty to thirty thousand dollar range, the added burden would amount to 12%.

Indeed, repeal of the third year of the tax cut and indexing would cost the typical median income ($24,300 in 1980) family of four $1061 in higher taxes over the next three years and $3549 in higher taxes through 1988.

Now what, may I ask, is fair about any of that?

There are congressmen who want to scuttle the tax cut for the same reason they want to deliver indexing stillborn -- because their own appetite for spending money -- taxpayer money -- is out of control. Inflation may be a public enemy to the rest of us, but to them, it's an unwitting ally, because it artificially raises revenue by elevating working people into higher tax brackets. Lincoln used to tell about an Illinois politician who was once offered transport out of town on the nearest rail. And he replied that if it weren't for the honor of the thing, he's just as soon walk. Well, the average worker in this country can do just fine without the dubious honor of bracket creep. And if we mean business in bringing genuine reform as well as lasting recovery, then we will hold to the policies that promise both.

We will continue to apply self-discipline in the budgetary process, to whittle way at the growth rate of entitlement and other programs that have outstripped the ability of our economy to support them. We will scrutinize every federal expenditure for its usefulness, weighed against the danger of mountainous deficits. And we will not yield to special interests, whether in pinstripes or bluejeans, who distort the truth for their own selfish ends. You've all heard of bankers' hours. Well, these days, some bankers are working over time -- not to attract customers but to frighten them. Their arguments against withholding of interest and dividend income, I'm sorry to say, are about as phony as a three dollar bill. This is not a new tax, nor an unfair burden on financial institutions. It is tax reform, tax compliance, and the principle of equal treatment carried beyond the rhetoric of election years. The auto worker has his taxes deducted from each week's paycheck. Why shouldn't those with unearned income accept a similar deduction once a year? At a time when sacrifice has been asked and given by the many, I can see no justification for exempting the few.

In the end, however, the renewal of American industry will come about, not because Washington wished it, but because economic managers in the field willed it. We have come through a recession which, ironically, has left much of American industry in better condition to compete, to innovate, to scratch out or expand its share of tomorrow's market. America stands poised for renewal. Yet all our progress could vanish with hardly a trace if American business loses its nerve or abandons its taste for competition -- if American workers forget the harsh lessons of inflation and joblessness taught over a decade or more of immoderate demands -- if government owns up to its own responsibilities, only to have business run away from possibility.

Not long ago, I had a chance to review the findings of a Cambridge-based think tank, the Strategic Planning Institute. After surveying 200 major U.S. firms and their strategies for future operation, SPI discovered that American industry has yet to grasp possibilities over and above new technologies alone. Investment even now could be increased by 30%. For support, the authors point to Miller Brewing Company, eighth ranking brewer when Phillip Morris purchased it in 1970, with a market share of less than 5%. Over the next three years, Phillip Morris doubled plant capacity, designed new ad campaigns, and withstood one year of red ink in pursuit of a larger goal.

Today, Miller is the second largest company in its field, and a highly profitable Number Two at that. The implication is clear: our preoccupation with the short run has blinded us to the necessity for risktaking. Walter Bagehot put it bluntly yet truthfully more than a century ago. "The buoyant rise and rule," he wrote, "the weak, the shrinking, and the timid fall and serve."

And it appears to me that the auto industry, as well as many others, have used the hard times of recession to rediscover a fighting spirit of ingenuity. It may even be that the unrelenting pressure of foreign competition is having a beneficial effect on production methods and product development.

There are three big international issues which are affecting industrial centers like Detroit. The first is foreign competition and the accompanying protectionist pressures. Those pressures are producing some interesting results.

Chrysler, for example, finds it can produce twice as many cars now as at a time when its managerial staff was double the current size. Automakers are adopting the Japanese supply system known as kanban, eliminating the costly inefficiency of huge parts inventories and forcing suppliers to improve their own quality. Along with scar tissue comes wisdom. And Detroit is leading the way in applying managerial ingenuity to meeting and beating their foreign competition.

These signs of managerial vigor don't square with the calls for protectionism that seek to turn back the clock. Commenting on the inevitable march of history, Omar Khayyham once wrote: "the moving finger writes, and having writ, moves on." We cannot go back to those pioneering days of only a few decades ago when "major markets" were defined as New York or Chicago. Today your markets are worldwide and protectionism implies trade ramifications that lead directly to more unemployment in Detroit and throughout the country.

The second big issue is oil.

Today we have a new OPEC agreement on oil pricing. This is clearly good news for the United States and the world economy. It will mean less inflation, which will hold interest rates down, and hopefully, car sales up.

The oil price reduction will obviously place some strains on certain oil exporters with large external debts. However, of the ten nations with the largest debts, eight are oil importers. This action will be of great benefit to them as well as to the other less developed countries. Those are repercussions the Treasury is watching very closely.

The third issue is international debt and the role of the International Monetary Fund -- the IMF.

Right now the Administration is seeking Congressional approval of an increase in quotas for the IMF -- an increase which is acutely needed for the IMF to continue its traditional role in international lending.

If there was too much international lending in the decade of the 70's that contributed to today's problems, too little lending in the 80's would be disastrous. The key here is to pursue a prudent and balanced approach.

Many have asked: What difference does international lending make to us? The short answer is that it makes a tremendous difference, because the ability of these countries to successfully adjust to their new realities will have a direct and powerful impact on economic activity here in the United States.

U.S. exports in 1980 accounted for 19 percent of total production of goods compared to only 9 percent ten years earlier. And during the same period, export-related jobs rose 75 percent, to over 5 million.

Let me cite Mexico as an immediate case in point.

Mexico is our third largest trading partner, after Canada and Japan. And, as recently as 1981, it was a partner with whom we had an export boom and a substantial trade surplus. This situation changed dramatically in 1982, as Mexico began experiencing severe debt and liquidity problems. As a result, U.S. exports to Mexico dropped by a staggering 60 percent between the fourth quarter of 1981 and the fourth quarter of 1982. Our $4 billion trade surplus with Mexico in 1981 was transformed into a trade deficit of nearly $4 billion in 1982, due mainly to an annual average drop in U.S. exports of one-third. This $8 billion deterioration was our worst swing in trade performance with any country in the world, and it was due almost entirely to the financing problem.

We believe that this situation will start to turn around, and we can begin to resume more normal exports to Mexico. If this happens, it will be due in large part to the fact that, late in December, an IMF program for Mexico went into effect. This program and the financing associated with it will permit resumption of more normal levels of economic activity and imports. Without the IMF program, all we could look forward to would be ever-deepening depression in Mexico and still further declines in our exports to that country. Improvement in the Mexican situation will translate directly into more jobs in the U.S.

And there is a second way in which all this affects us.

What if debtor nations cannot service their debts? If interest payments to U.S. banks are more than 90 days late, the banks stop accruing them on their books, they suffer reduced profits and bear the costs of continued funding of the loan. Provisions may have to be made for loss, and as loans are actually written off, the capital of the bank is reduced. In that case the creditors banks' capital/asset ratios would shrink. American banks would then have to take measures to restore the capital/asset ratios. Banks would be forced to make fewer loans to all borrowers, domestic and foreign. Auto loans in Detroit, housing loans in Dallas, capital expansion loans in California -- all would be affected.

Thus we must look to this period of recovery as a time of great transition and opportunity. A good deal of restructuring has taken place during this long and troubling world recession -- restructuring of our industrial capacity at home and restructuring of our international relationships as well. We approach a time of renewal.

"This is perhaps the most beautiful time in human history," Dr. Jonas Salk has written. "It is really pregnant with all kinds of creative possibilities made possible by science and technology which now constitute the slave of man -- if man is not enslaved by it."

Therein lies the ultimate challenge of change. How we meet that challenge will be influenced by political decisions, to be sure. But whether you choose to see calamity or potential will also help to decide what the rest of us see a few years down the road. The President has done much to foster a climate ripe for innovation. But we cannot innovate for the business community. We can only echo the sentiment of Emerson, who said, "Be an opener of doors for such as come after thee, and do not try to make the universe a blind alley."

The doors, ladies and gentlemen, have been opened. We invite you to walk through them, and to join us in opening them still wider for those who follow. We invite you to convert recovery into renewal, for Detroit and all across this enterprising land.

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federal financing bank NEWS
WASHINGTON, D.C. 20220
Press inquiries: 202-566-2615

FOR IMMEDIATE RELEASE March 15, 1983

FEDERAL FINANCING BANK ACTIVITY

Francis X. Cavanaugh, Secretary, Federal Financing Bank (FFB), announced the following activity for the month of January 1983.

FFB holdings of obligations issued, sold, or guaranteed by other Federal agencies on January 31, 1983 totaled $126.6 billion, an increase of almost $0.2 billion over the level on December 31, 1982. FFB increased holdings of agency guaranteed debt by over $0.4 billion. Holdings of agency debt issues decreased by $0.1 billion and agency assets purchased decreased by $0.2 billion. A total of 260 disbursements were made during the month.

Attached to this release are tables presenting FFB January loan activity; new FFB commitments to lend during January and FFB holdings as of January 31, 1983.

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R-2087

JANUARY 1983 ACTIVITY

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
ON-BUDGET AGENCY DEBT					
TENNESSEE VALLEY AUTHORITY					
Power Bond 1983 A	1/6	$ 150,000,000.00	1/31/13	10.575%	
Note #276	1/6	205,000,000.00	3/31/83	8.351%	
Note #277	1/7	170,000,000.00	5/5/83	8.446%	
Note #278	1/14	30,000,000.00	5/5/83	8.113%	
Note #279	1/21	10,000,000.00	5/5/83	8.214%	
Note #280	1/31	5,000,000.00	5/5/83	8.394%	
NATIONAL CREDIT UNION ADMINISTRATION					
Central Liquidity Facility					
Note #149	1/10	2,000,000.00	3/1/83	8.122%	
+Note #150	1/12	12,000,000.00	4/12/83	8.045%	
Note #151	1/14	500,000.00	4/12/83	8.022%	
+Note #152	1/28	7,450,000.00	3/3/83	8.391%	
+Note #153	1/28	7,000,000.00	5/27/83	8.465%	
OFF-BUDGET AGENCY DEBT					
UNITED STATES RAILWAY ASSOCIATION					
*Note #31	1/3	80,203,499.11	3/31/83	8.280%	
AGENCY ASSETS					
FARMERS HOME ADMINISTRATION					
Certificates of Beneficial Ownership					
	1/7	90,000,000.00	1/7/03	10.805%	11.097% ann.
	1/7	250,000,000.00	1/7/98	10.555%	10.834% ann.
	1/31	120,000,000.00	1/31/98	10.885%	11.181% ann.
DEPARTMENT OF HEALTH & HUMAN SERVICES					
Health Maintenance Organization Notes					
Block #27	1/26	1,632,634.40	7/1/01-7/1/04	10.955%	
GOVERNMENT - GUARANTEED LOANS					
DEPARTMENT OF DEFENSE - FOREIGN MILITARY SALES					
Indonesia 8	1/5	450,000.00	5/5/91	10.105%	
Israel 8	1/5	2,016,479.74	9/1/09	10.735%	
Turkey 9	1/5	221,290.89	6/22/92	10.475%	
Indonesia 7	1/6	1,343,873.52	3/20/90	10.336%	
Philippines 7	1/6	1,694,546.19	9/10/87	8.456%	
Dominican Republic 5	1/7	63,827.21	4/30/89	10.344%	
Greece 14	1/7	6,393,006.67	4/30/11	10.515%	
Liberia 9	1/7	2,579.66	7/21/94	10.515%	
Egypt 3	1/10	981,962.67	6/15/12	10.722%	
Korea 15	1/10	771,391.62	12/31/93	10.395%	
El Salvador 5	1/11	2,306,974.40	11/30/94	10.118%	
El Salvador 5	1/12	205,165.08	11/30/94	10.205%	
Jordan 8	1/12	690,006.62	11/22/90	8.885%	
Botswana 1	1/13	23,852.96	1/15/87	8.285%	
Greece 12	1/13	2,812,854.00	6/3/10	10.744%	
Greece 13	1/13	1,939,956.00	9/22/90	10.159%	
Israel 8	1/13	500,000.00	9/1/09	10.755%	
Indonesia 7	1/14	302,094.00	3/20/90	10.165%	
Indonesia 8	1/14	3,355,860.00	5/5/91	9.908%	
Jordan 8	1/14	1,092,899.47	11/21/90	8.918%	
Liberia 9	1/14	289,634.54	7/21/94	10.391%	
Thailand 9	1/14	1,293,587.00	9/15/93	10.372%	

+rollover
*maturity extension

BORROWER		DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
DEPARTMENT OF DEFENSE - FOREIGN MILITARY SALES (Cont'd)						
Turkey 9		1/14	$ 486,067.42	6/22/92	10.375%	
Egypt 3		1/17	15,626,164.77	6/15/12	10.695%	
Turkey 9		1/17	1,849,053.04	6/22/92	10.375%	
Indonesia 7		1/17	712,032.00	3/20/90	10.138%	
Israel 13		1/18	2,879,107.89	2/16/12	10.745%	
Israel 13		1/19	43,633,690.96	2/16/12	10.787%	
Greece 14		1/20	263,750.00	4/30/11	10.545%	
Israel 8		1/20	80,000,000.00	9/1/09	10.903%	
Jordan 8		1/20	1,207,394.48	11/22/90	9.235%	
Malaysia 5		1/20	2,232,878.44	2/20/86	9.438%	
Malaysia 6		1/20	3,300,468.78	9/10/87	8.545%	
Greece 13		1/24	3,912,750.28	9/22/90	10.415%	
Grecee 14		1/24	6,400,000.00	4/30/11	10.735%	
Somalia 1		1/24	205,628.26	9/1/92	10.715%	
Egypt 3		1/25	3,189,490.38	6/15/12	11.069%	
Israel 8		1/26	757,007.91	9/1/09	11.155%	
Israel 13		1/26	11,987,803.58	2/16/12	11.041%	
Honduras 9		1/27	2,638,626.12	9/20/94	10.817%	
Turkey 9		1/27	268,248.21	6/22/92	10.795%	
Egypt 3		1/28	1,906,518.06	6/15/12	11.045%	
Jamaica 1		1/28	311,789.66	3/1/93	10.785%	
Jamaica 2		1/28	83,750.72	12/20/93	10.791%	
Kenya 10		1/28	251,451.00	5/5/94	9.987%	
Panama 4		1/28	773,593.20	5/25/89	10.115%	
Lebanon 4		1/31	9,311,481.00	7/25/89	10.126%	
Turkey 9		1/31	700,000.00	6/22/92	10.805%	
DEPARTMENT OF ENERGY						
Geothermal Loan Guarantees						
Northern California Municipal Power Company #2		1/3	3,407,240.27	10/1/83	8.795%	8.700% qtr.
Synthetic Fuels Guarantees - Non-Nuclear Act						
Great Plains Gasification Assoc.	#45A	1/3	22,500,000.00	4/1/83	9.270%	
	#45B	1/3	28,500,000.00	7/1/83	9.445%	
	#45C	1/3	22,500,000.00	1/2/84	9.675%	
	#46	1/10	14,000,000.00	7/1/83	9.225%	
	#47	1/17	15,500,000.00	1/2/84	9.215%	
	#48	1/24	7,000,000.00	1/2/84	9.505%	
	#49	1/31	11,500,000.00	7/1/83	9.295%	
DEPARTMENT OF HOUSING & URBAN DEVELOPMENT						
Community Development Block Grant Guarantees						
Phila. Auth. for Ind. Dev.		1/3	100,000.00	10/1/03	10.666%	10.950% ann.
*Lawrence, MA		1/3	1,138,400.00	1/1/88	10.258%	10.521% ann.
Buffalo, NY		1/5	345,000.00	8/1/83	10.584%	10.864% ann.
Hammond, IN		1/7	155,273.00	5/1/84	9.025%	9.229% ann.
Baldwin Park, CA		1/7	177,900.00	8/15/84	9.255%	9.469% ann.
Oakland, CA		1/7	450,000.00	9/1/03	10.625%	10.907% ann.
Wilmington, DE		1/7	172,000.00	1/15/04	10.637%	10.920% ann.
Washington County, PA		1/20	44,348.35	8/1/83	8.375%	8.397% ann.
Oakland, CA		1/24	240,000.00	9/1/03	10.855%	11.150% ann.
Buffalo, NY		1/26	467,000.00	8/1/03	10.875%	11.171% ann.
Syracuse Ind. Dev. Agency		1/26	144,000.00	7/1/03	10.871%	11.166% ann.
Phila. Auth. for Ind. Dev.		1/28	1,175,400.00	10/1/03	10.937%	11.236% ann.
Washington County, PA		1/28	30,111.30	8/1/83	8.625%	8.633% ann.
Mayaguez, PR		1/28	175,750.00	8/1/83	8.675%	8.683% ann.
Public Housing Notes						
Sale #29		1/7	27,312,427.06	11/1/08-11/1/19	10.624%	10.906% ann.

*maturity extension

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
NATIONAL AERONAUTICS AND SPACE ADMINISTRATION					
Space Communications Company	1/20	$ 9,000,000.00	10/1/92	10.240%	10.502% ann.
RURAL ELECTRIFICATION ADMINISTRATION					
*Big Rivers Electric #58	1/2	1,697,000.00	12/31/13	10.619%	10.482% qtr.
*Big Rivers Electric #91	1/2	512,000.00	12/31/13	10.619%	10.482% qtr
*S. Mississippi Electric #3	1/3	363,000.00	12/31/15	10.594%	10.457% qtr.
*S. Mississippi Electric #177	1/3	24,278,000.00	12/31/15	10.594%	10.457% qtr.
Western Illinois Power #225	1/3	10,491,000.00	12/31/17	10.600%	10.463% qtr.
S. Mississippi Electric #90	1/3	1,467,000.00	12/31/17	10.600%	10.463% qtr.
S. Mississippi Electric #171	1/3	11,493,000.00	12/31/17	10.600%	10.463% qtr.
Arkansas Electric #221	1/4	381,000.00	12/31/17	10.548%	10.412% qtr.
Arkansas Electric #142	1/4	1,712,000.00	12/31/17	10.548%	10.412% qtr.
*S. Illinois Power #38	1/4	100,000.00	12/31/14	10.549%	10.413% qtr.
Kansas Electric #216	1/6	3,662,000.00	12/31/17	10.634%	10.496% qtr.
*Arkansas Electric #142	1/6	6,890,000.00	12/31/15	10.633%	10.496% qtr.
*Colorado Ute Electric #168	1/6	4,426,000.00	1/6/85	9.525%	9.414% qtr.
*San Miguel Electric #110	1/7	6,218,000.00	1/7/85	9.515%	9.404% qtr.
°Ogden Telephone #72	1/7	3,500,000.00	12/31/11	10.658%	10.520% qtr.
Seminole Electric #141	1/7	9,456,000.00	12/31/17	10.658%	10.520% qtr.
*Cajun Electric #180	1/7	50,800,000.00	12/31/15	10.657%	10.519% qtr.
*Central Electric #128	1/8	1,341,000.00	1/8/85	9.385%	9.277% qtr.
*Deseret G&T #170	1/9	469,000.00	12/31/15	10.655%	10.516% qtr.
*Wolverine Electric #100	1/10	1,350,000.00	1/10/85	9.395%	9.287% qtr.
Wabash Valley Power #104	1/10	8,872,000.00	1/10/85	9.395%	9.287% qtr.
Wabash Valley Power #206	1/10	623,000.00	1/10/85	9.395%	9.287% qtr.
Deseret G&T #211	1/10	8,481,000.00	12/31/17	10.654%	10.515% qtr.
*N. Michigan Electric #101	1/10	1,263,000.00	1/10/85	9.395%	9.287% qtr.
°Sugar Land Telephone #69	1/12	942,000.00	12/31/13	10.639%	10.501% qtr.
°Sugar Land Telephone #69	1/12	945,000.00	12/31/15	10.640%	10.502% qtr.
°Sugar Land Telephone #69	1/12	682,000.00	12/31/15	10.640%	10.502% qtr.
°Sugar Land Telephone #69	1/12	1,626,000.00	12/31/15	10.640%	10.502% qtr.
Cajun Electric #147	1/12	51,000,000.00	12/13/17	10.639%	10.501% qtr.
*Colorado Ute Electric #8	1/12	4,500,000.00	12/31/11	10.642%	10.504% qtr.
*Wabash Valley Power #104	1/12	2,199,000.00	12/31/15	10.640%	10.502% qtr.
*Western Illinois Power #99	1/12	2,407,000.00	12/31/13	10.641%	10.503% qtr.
Brookeville Telephone #53	1/12	65,000.00	1/12/85	9.315%	9.209% qtr.
*N. Michigan Electric #183	1/13	583,000.00	1/13/85	9.345%	9.238% qtr.
*Cajun Electric #76	1/13	20,000,000.00	12/31/15	10.616%	10.479% qtr.
Hoosier Energy #107	1/13	7,224,000.00	1/13/85	9.345%	9.238% qtr.
Hoosier Energy #202	1/13	4,776,000.00	1/13/85	9.345%	9.238% qtr.
*Big Rivers Electric #136	1/14	168,000.00	12/31/15	10.605%	10.468% qtr.
*Big Rivers Electric #179	1/14	9,282,000.00	12/31/15	10.605%	10.468% qtr.
Associated Electric #132	1/14	6,300,000.00	12/31/17	10.605%	10.468% qtr.
*Western Illinois Power #162	1/15	4,017,000.00	12/31/15	10.643%	10.505% qtr.
*Deseret G&T #170	1/15	1,352,000.00	12/31/14	10.644%	10.506% qtr.
*Oglethorpe Power #74	1/15	29,884,000.00	12/31/14	10.644%	10.506% qtr.
*Oglethorpe Power #74	1/15	14,152,000.00	12/31/12	10.646%	10.508% qtr.
*Oglethorpe Power #150	1/15	18,776,000.00	12/31/14	10.644%	10.506% qtr.
Wabash Valley Power #252	1/17	1,352,000.00	1/17/85	9.225%	9.121% qtr.
New Hampshire Electric #192	1/17	902,000.00	1/17/85	9.225%	9.121% qtr.
Basin Electric Power #137	1/17	20,000,000.00	1/17/85	9.225%	9.121% qtr.
Western Farmers Electric #133	1/17	725,000.00	1/17/85	9.225%	9.121% qtr.
Western Farmers Electric #133	1/17	2,700,000.00	1/17/85	9.225%	9.121% qtr.
East Kentucky Power #188	1/17	1,200,000.00	12/31/17	10.642%	10.504% qtr.
*Alabama Electric #26	1/17	7,000,800.00	12/31/13	10.645%	10.507% qtr.
Chugach Electric #204	1/18	1,350,000.00	12/31/17	10.638%	10.501% qtr.
*Seminole Electric #141	1/18	12,372,000.00	12/31/14	10.641%	10.503% qtr.
Brazos Electric #108	1/19	277,000.00	12/31/17	10.694%	10.555% qtr.
Brazos Electric #230	1/19	5,520,000.00	12/31/17	10.694%	10.555% qtr.
*Colorado Ute Electric #96	1/19	708,000.00	1/19/85	9.265%	9.160% qtr.
*Soyland Power #165	1/19	4,135,000.00	1/19/85	9.265%	9.160% qtr.
*Ponderosa Telephone #35	1/19	99,000.00	1/19/85	9.265%	9.160% qtr.
Brookeville Telephone #53	1/19	1,225,000.00	12/31/15	10.696%	10.557% qtr.
*S. Mississippi Electric #3	1/19	230,000.00	12/31/13	10.698%	10.559% qtr.
*S. Mississippi Electric #3	1/20	6,300,000.00	12/31/10	10.810%	10.668% qtr.

°early extension
*maturity extension

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
RURAL ELECTRIFICATION ADMINISTRATION (Cont'd)					
*S. Mississippi Electric #3	1/20	$ 709,000.00	12/31/15	10.805%	10.663% qtr.
Tri-State G&T #157	1/20	1,721,000.00	12/31/17	10.804%	10.661% qtr.
Big Rivers Electric #91	1/21	1,095,000.00	12/31/17	10.801%	10.659% qtr.
Big Rivers Electric #143	1/21	3,092,000.00	12/31/17	10.801%	10.659% qtr.
Big Rivers Electric #179	1/21	1,007,000.00	12/31/17	10.801%	10.659% qtr.
Seminole Electric #141	1/21	35,007,000.00	12/31/17	10.801%	10.659% qtr.
°San Miguel Electric #110	1/21	128,309,000.00	12/31/12	10.805%	10.663% qtr.
°San Miguel Electric #110	1/21	20,000,000.00	12/31/13	10.804%	10.662% qtr.
°San Miguel Electric #110	1/21	12,000,000.00	12/31/13	10.804%	10.662% qtr.
°San Miguel Electric #110	1/21	10,000,000.00	12/31/13	10.804%	10.662% qtr.
°San Miguel Electric #110	1/21	17,824,000.00	12/31/13	10.804%	10.662% qtr.
°San Miguel Electric #205	1/21	35,000,000.00	12/31/15	10.803%	10.661% qtr.
°San Miguel Electric #205	1/21	12,100,000.00	12/31/15	10.803%	10.661% qtr.
°San Miguel Electric #205	1/21	10,900,000.00	12/31/16	10.801%	10.659% qtr.
°San Miguel Electric #205	1/21	11,400,000.00	12/31/16	10.802%	10.660% qtr.
°Basin Electric #137	1/21	10,000,000.00	12/31/15	10.802%	10.660% qtr.
*Colorado Ute Electric #71	1/21	1,850,000.00	1/21/85	9.395%	9.287% qtr.
*Big Rivers Electric #58	1/21	605,000.00	12/31/15	10.802%	10.660% qtr.
*Big Rivers Electric #91	1/21	2,971,000.00	12/31/15	10.802%	10.660% qtr.
*Big Rivers Electric #136	1/21	72,000.00	12/31/15	10.802%	10.660% qtr.
*Big Rivers Electric #143	1/21	10,000.00	12/31/15	10.802%	10.660% qtr.
*Big Rivers Electric #179	1/21	7,475,000.00	12/31/15	10.802%	10.660% qtr.
*Big Rivers Electric #91	1/21	3,265,000.00	12/31/13	10.927%	10.782% qtr.
*Big Rivers Electric #58	1/22	1,146,000.00	12/31/13	10.927%	10.782% qtr.
*E. Kentucky Power #73	1/22	6,371,000.00	12/31/13	10.927%	10.782% qtr.
*N. Michigan Electric #183	1/22	232,000.00	1/22/85	9.585%	9.473% qtr.
*Cajun Electric #76	1/22	50,000,000.00	1/22/85	9.585%	9.473% qtr.
*Alabama Electric #26	1/23	12,726,000.00	12/31/15	10.926%	10.781% qtr.
Colorado Ute Eletric #96	1/24	230,000.00	1/24/85	9.595%	9.483% qtr.
Oglethorpe Power #74	1/24	42,597,000.00	12/31/17	10.925%	10.780% qtr.
Sitka Telephone #213	1/24	4,307,093.00	1/24/85	9.595%	9.483% qtr.
*San Miguel Electric #110	1/25	9,005,000.00	1/25/85	9.665%	9.551% qtr.
*Cooperative Power #121	1/26	1,102,000.00	12/31/15	10.960%	10.814% qtr.
*S. Mississippi Electric #4	1/26	244,000.00	12/31/13	10.962%	10.816% qtr.
Western Illinois Power #225	1/26	3,628,000.00	12/31/17	10.958%	10.812% qtr.
Basin Electric #137	1/26	20,000,000.00	1/26/85	9.565%	9.453% qtr.
*S. Mississippi Electric #90	1/26	680,000.00	12/31/13	10.961%	10.815% qtr.
*S. Mississippi Electric #3	1/26	316,000.00	12/31/13	10.961%	10.815% qtr.
Colorado Ute Electric #168	1/27	4,418,000.00	1/27/85	9.645%	9.531% qtr.
Quaker State Telephone #92	1/27	1,000,000.00	12/31/17	11.058%	10.909% qtr.
Kansas Electric #216	1/27	300,000.00	12/31/17	11.058%	10.909% qtr.
North Carolina Electric #185	1/28	6,241,000.00	1/28/85	9.615%	9.502% qtr.
*Hoosier Energy #107	1/30	30,000,000.00	1/30/85	9.615%	9.502% qtr.
*Basin Electric #87	1/30	528,000.00	12/31/15	11.039%	10.891% qtr.
*San Miguel Electric #110	1/30	8,152,000.00	1/30/85	9.615%	9.502% qtr.
*Wolverine Electric #132	1/30	459,000.00	1/30/85	9.615%	9.502% qtr.
*Upper Missouri G&T #172	1/30	1,870,000.00	1/30/85	9.615%	9.502% qtr.
Basin Electric #232	1/31	228,000.00	1/31/85	9.615%	9.502% qtr.
Tex-La Electric #208	1/31	600,000.00	1/31/85	9.615%	9.502% qtr.
Plains Electric G&T #158	1/31	4,038,000.00	12/31/17	11.038%	10.890% qtr.
*Allegheny Electric #93	1/31	5,432,000.00	1/31/85	9.615%	9.502% qtr.
*Allegheny Electric #93	1/31	1,443,000.00	1/31/85	9.615%	9.502% qtr.
*Allegheny Electric #175	1/31	1,708,000.00	1/31/85	9.615%	9.502% qtr.
*Southern Illinois Power #38	1/31	1,880,000.00	12/31/12	11.042%	10.893% qtr.
SMALL BUSINESS ADMINISTRATION					
Small Business Investment Company Debentures					
Associated Capital Corp.	1/19	550,000.00	1/1/86	9.485%	
Sprout Capital Corp.	1/19	1,000,000.00	1/1/86	9.485%	
North Star Ventures, Inc.	1/19	750,000.00	1/1/93	10.405%	
State & Local Development Company Debentures					
Cleveland Area Dev. Fin. Corp.	1/5	31,000.00	1/1/98	10.385%	
St. Louis Local Dev. Co.	1/5	36,000.00	1/1/98	10.385%	
Allentown Econ. Dev. Corp.	1/5	47,000.00	1/1/98	10.385%	

*early extension

BORROWER	DATE	AMOUNT OF ADVANCE	FINAL MATURITY	INTEREST RATE (semi-annual)	INTEREST RATE (other than semi-annual)
State & Local Development Company Debentures (Cont'd)					
St. Louis Local Dev. Co.	1/5	$ 65,000.00	1/1/98	10.385%	
Columbus Countywide Dev. Corp.	1/5	70,000.00	1/1/98	10.385%	
Commonwealth SBD Corp.	1/5	109,000.00	1/1/98	10.385%	
BEDCO Dev. Corp.	1/5	125,000.00	1/1/98	10.385%	
Springfield SBA Inc.	1/5	147,000.00	1/1/98	10.385%	
Springfield SBA Inc.	1/5	160,000.00	1/1/98	10.385%	
City-Wide SBD Corp.	1/5	186,000.00	1/1/98	10.385%	
Areawide Dev. Corp.	1/5	236,000.00	1/1/98	10.385%	
Cleveland Area Dev. Fin. Corp.	1/5	288,000.00	1/1/98	10.385%	
Atlanta Local Dev. Co.	1/5	455,000.00	1/1/98	10.385%	
Central Ozarks Dev. Inc.	1/5	18,000.00	1/1/03	10.509%	
Grand Rapids Local Dev. Corp.	1/5	38,000.00	1/1/03	10.509%	
First Alabama Dev. Corp.	1/5	59,000.00	1/1/03	10.509%	
St. Louis Local Dev. Co.	1/5	60,000.00	1/1/03	10.509%	
S. Central Illinois RP & DC	1/5	60,000.00	1/1/03	10.509%	
Greater Southwest Loc. Dev. Co.	1/5	63,000.00	1/1/03	10.509%	
Lake County Dev. Corp.	1/5	65,000.00	1/1/03	10.509%	
South Georgia Area Dev. Corp.	1/5	75,000.00	1/1/03	10.509%	
West Contra Costa Loc. Dev. Co.	1/5	84,000.00	1/1/03	10.509%	
Forward Dev. Corp.	1/5	85,000.00	1/1/03	10.509%	
Louisville Economic Dev. Corp.	1/5	92,000.00	1/1/03	10.509%	
Plymouth Industrial Dev. Corp.	1/5	95,000.00	1/1/03	10.509%	
Corp. for Econ. Dev. in Des Moines	1/5	122,000.00	1/1/03	10.509%	
Grand Rapids Loc. Dev. Corp.	1/5	126,000.00	1/1/03	10.509%	
New Haven Community Invest. Corp.	1/5	130,000.00	1/1/03	10.509%	
Eastern Maine Dev. District	1/5	139,000.00	1/1/03	10.509%	
Texas Certified Dev. Co. Inc.	1/5	204,000.00	1/1/03	10.509%	
Texas Certified Dev. Co. Inc.	1/5	218,000.00	1/1/03	10.509%	
Eastern Maine Dev. District	1/5	236,000.00	1/1/03	10.509%	
Ocean SBD Authority Inc.	1/5	240,000.00	1/1/03	10.509%	
Atlanta Loc. Dev. Co.	1/5	256,000.00	1/1/03	10.509%	
Metropolitan Growth & Dev. Corp.	1/5	265,000.00	1/1/03	10.509%	
Bedco Dev. Corp.	1/5	275,000.00	1/1/03	10.509%	
Texas Certified Dev. Co. Inc.	1/5	314,000.00	1/1/03	10.509%	
Forward Dev. Corp.	1/5	336,000.00	1/1/03	10.509%	
Long Island Dev. Corp.	1/5	480,000.00	1/1/03	10.509%	
Tucson Local Dev. Corp.	1/5	53,000.00	1/1/08	10.576%	
Jefferson County Dev. Corp.	1/5	55,000.00	1/1/08	10.576%	
Metro SBA Corp.	1/5	70,000.00	1/1/08	10.576%	
Miami Citywide Dev. Inc.	1/5	86,000.00	1/1/08	10.576%	
New Haven Community Inv. Corp.	1/5	90,000.00	1/1/08	10.576%	
Cleveland Area Dev. Fin. Corp.	1/5	113,000.00	1/1/08	10.576%	
Wisconsin Bus. Dev. Fin. Corp.	1/5	145,000.00	1/1/08	10.576%	
Columbus Countywide Dev. Corp.	1/5	186,000.00	1/1/08	10.576%	
Central Ozarks Dev. Inc.	1/5	190,000.00	1/1/08	10.576%	
Cleveland Citywide Dev. Corp.	1/5	210,000.00	1/1/08	10.576%	
New Orleans Citywide Dev. Corp.	1/5	340,000.00	1/1/08	10.576%	
Greater Salt Lake Bus. District	1/5	436,000.00	1/1/08	10.576%	
Department of Transportation					
National Railroad Passenger Corporation					
Note #31	1/3	25,106,237.04	4/1/83	8.280%	
Note #31	1/18	2,607,531.00	4/1/83	8.002%	

FEDERAL FINANCING BANK
JANUARY 1983 Commitments

BORROWER	GUARANTOR	AMOUNT	COMMITMENT EXPIRES	MATURITY
Pakistan	DOD	$ 150,000,000.00	1/15/85	1/15/95
Somalia	DOD	10,000,000.00	11/30/84	11/30/12
Lebanon	DOD	10,000,000.00	1/25/85	1/25/91
Wilimington, DE	HUD	1,000,000.00	1/15/84	1/15/04
Oakland, CA	HUD	2,000,000.00	9/1/83	9/1/03
San Buenaventura, CA	HUD	1,000,000.00	8/15/84	8/15/84
Mayaguez, PR	HUD	1,242,080.00	8/1/83	8/1/87

FEDERAL FINANCING BANK HOLDINGS
(in millions)

Program	January 31, 1983	December 31, 1982	Net Change 1/1/83-1/31/83	Net Change 10/1/82-1/31/83
On-Budget Agency Debt				
Tennessee Valley Authority	$ 12,640.0	$ 12,640.0	$ -0-	$ 355.0
Export-Import Bank	14,176.7	14,176.7	-0-	222.7
NCUA-Central Liquidity Facility	100.0	103.0	-2.9	-30.0
Off-Budget Agency Debt				
U.S. Postal Service	1,221.0	1,221.0	-0-	-0-
U.S. Railway Association	121.9	194.3	-72.4	-73.0
Agency Assets				
Farmers Home Administration	53,056.0	53,261.0	-205.0	-680.0
DHHS-Health Maintenance Org.	118.4	116.8	1.6	-12.7
DHHS-Medical Facilities	148.8	148.8	-0-	3.0
Overseas Private Investment Corp.	18.5	19.4	-.9	-3.0
Rural Electrification Admin.-CBO	3,123.7	3,123.7	-0-	-0-
Small Business Administration	55.4	56.1	-.6	-2.6
Government-Guaranteed Loans				
DOD-Foreign Military Sales	12,446.3	12,279.1	167.2	1,010.4
DEd.-Student Loan Marketing Assn.	5,000.0	5,000.0	-0-	-0-
DOE Geothermal Loans	44.3	40.9	3.4	7.7
DOE-Non-Nuclear Act (Great PLains)	547.0	476.5	70.5	207.0
DHUD-Community Dev. Block Grant	128.7	125.8	2.9	11.7
DHUD-New Communities	33.5	33.5	-0-	-0-
DHUD-Public Housing Notes	1,703.0	1,675.7	27.3	78.7
General Services Administration	419.1	419.1	-0-	-1.4
DOI-Guam Power Authority	36.0	36.0	-0-	-0-
DOI-Virgin Islands	29.2	29.5	-.3	-.3
NASA-Space Communications Co.	823.3	814.3	9.0	65.5
Rural Electrification Admin.	17,329.9	17,156.7	173.2	1,048.4
SBA-Small Business Investment Cos.	728.4	732.1	-3.8	16.4
SBA-State/Local Development Cos.	75.4	67.4	8.0	27.0
TVA-Seven States Energy Corp.	1,243.0	1,257.2	-14.2	-14.9
DOT-Amtrak	855.7	855.0	.6	.3
DOT-Title V, RRRR Act	186.4	188.0	-1.6	-6.5
DOT-WMATA	177.0	177.0	-0-	-0-
TOTALS*	$ 126,586.6	$ 126,424.4	$ 162.1	$ 2,229.3

*figures may not total due to rounding

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE UPON DELIVERY
Wednesday, March 16, 1983

REMARKS BY DONALD T. REGAN
SECRETARY OF THE TREASURY
BEFORE
THE NATIONAL COUNCIL ON AGING ANNUAL CONVENTION
DETROIT, MICHIGAN
WEDNESDAY, MARCH 16, 1983

I want you know how pleased I am to be with you today to discuss information of vital importance to every older American. But before I ask you to look with me at facts too often obscured by partianship and political posturing, I want to present you with a quotation. Here it is:

"The world has never seen anything like it before. The progress of the ages almost outstrips human belief."

That's a quote fit for the celebration of a flight into space? Or perhaps a tribute to genetic engineering? But, it was just Daniel Webster in the 1800's celebrating the laying of a few more miles of railroad track in New Hampshire. To us that might seem like rhetorical overkill. There certainly aren't many events that deserve such acclaim.

But there is one success today that unquestionably fits Webster's composition. It is the historically unprecedented achievement of a longer lifespan, of years of retirement after a career, of retirement years that can offer new horizons of fulfillment and happiness.

No, I don't think Webster would have been so surprised at space shuttles, men on the moon, computerized offices, or even such marvels as the electric pencil sharpener. He clearly saw all that waiting somewhere along those railroad tracks. But I believe he would be simply astounded that after 40 years of active working life, which itself follows a dozen years of formal education, an American in 1980 could look forward to many years of something yet undreamed of in the time of Webster, a period called retirement.

But if he might be amazed at this fact, I believe he would be struck dumbfounded by discovering that this incredible achievement, this tribute to scientific research, this basic index of the quality of American life, is considered by many, not as a splendid success, but as a problem.

Let me say right off that I don't see this brilliant achievement as a problem. And this Administration doesn't see it as a problem. We view the 26-million Americans age 65 and older as offering our society, our government, our economic policy an opportunity to demonstrate both imagination and equity. Even more important, I see the wisdom and experience that resides in this segment of our population as a vital resource that we simply must call upon to help assure that this nation does not stumble back into policies and programs that could threaten what older Americans have spent a lifetime in constructing.

So, I am here today not to wring my hands about the so-called problems of Social Security and government finances. I am here today to provide some plain facts and to talk in common sense terms about what those facts mean.

Let's begin with Social Security. What happened to what was rightly considered the best achievement of the New Deal? I'll tell you exactly what happened to it. It was almost mortally wounded by the same force that supposedly pave the road to hell--good intentions. I know that no one needs to tell this audience, which understands the lessons of a long lifetime of experience, that good intentions mixed with muddled thinking is a prescription for disaster. To work well public policy needs a combination of good intentions and clear thinking.

Social security was, in part, a response to the Great Depression when many individuals lost most or all of their savings. Its original intent was to provide a basic pension to retired workers in commerce and industry. The decision was also made to sell the program as a private pension, rather than the tax and transfer system that it is. This perhaps "good intentioned" belief still causes problems today because some beneficiaries think the checks they receive are from their own personal savings account, rather than tax dollars paid by people currently working.

In the early days of the program, workers far outnumbered persons collecting benefits. With an excess of tax dollars over benefits paid out, the social security trust funds built reserves. These reserves were taken as an indication of the good health of the system and used as a justification to increase benefits in real terms as well to adjust for inflation.

In 1972, a major increase in benefits occurred. The Congress raised benefit levels by 20 percent and instituted an automatic indexing of the benefit formula. The purpose of automatic indexing was well intentioned -- it was to allow benefits to keep pace with inflation.

This rapid expansion in beneits was occurring at the same time the economy was experiencing slow growth and high inflation. Workers, whose contributions to social security pay benefits, found their real wages deteriorating. With benefits over the last 10 years being paid out faster than tax revenues came in, social security was placed in the precarious position you now hear about.

What we need now is a combination of good intentions with clear thinking. And that is precisely why the President has welcomed the recommendations of the Commission on Social Security. That is why he has urged Congress to transform those recommendations into law. That is why his position has attracted bi-partisan support--from Speaker O'Neill, Majority Leader Wright, Chairman Pepper, Senate Majority Leader Baker, Senate Finance Chairman Dole, House Majority Leader Michel.

Although this bi-partisan compromise rescue package doesn't please everyone --compromises never do--with one exception (which I will explore with you in a moment) they will save the Social Security Trust Fund. They will save it by:

...preserving the financial integrity of Social Security;

...ensuring that benefits are not cut below current levels; and

...fairly, equitably dealing with future funding requirements.

What is the exception I mentioned? That exception, the one force that could threaten to make a mockery of this hard won compromise, that could not just injure but ultimately ravage and destroy Social Security as an affordable Federal Policy, is a return of inflation.

Inflation is to a healthy society what fever is to an individual. It may give you rosy cheeks, but if allowed to rise high enough, it can consume your insides. When this Administration took office inflation was not only at levels never before encountered during peace time, but it had hit double-digits and, worse, seemed out of control. No one then in authority appeared to know how to stop it or was capable of doing so. Let us never forget that this Administration was called to office at least partially because the President promised the American people that he would stop inflation, and could stop it. And he has, in the face of what may be the largest population of doubting Thomases ever assembled, more than fulfilled his promise.

Where inflation was 12.4 percent when he took the oath of office; today it is at 3.9 percent, and falling. Getting from a sickening rate of inflation, to disinflation, and on the way to stability has not been painless. We all know that. But it also has not been the result of accident.

Our success with inflation has been the direct result of policies pursued by this Administration. We have cooperated with the Federal Reserve in their efforts to slow the growth of the money supply, thereby reducing the inflationary expectations which had fueled wage and price growth for so long. We have also acted to curtail government spending and regulation in order to free private sector initiative and increase business productivity. Finally, we enacted the largest tax cut in history--a tax cut that, even when last year's business tax adjustments are considered, totals $446 billion dollars. In addition to the tax relief and incentive provided young and old alike, there was another and absolutely fundamental feature of the 1981 tax cut--indexing or, for those who like an extra syllable, indexation--slated by law to begin in 1985.

Now what is indexing? Essentially it follows the same principle of cost of living adjustments in Social Security and other programs. As the cost of living goes up, pensions have been adjusted to assure the same return in real money. Indexation achieves the same end by moving in a reverse direction.

If inflation threatens to do what it did all throughout the 1970's--push people into higher tax brackets and thus serve as a hidden tax increase--indexing requires tax rates to be adjusted to compensate for the decline in the value of the dollar.

Indexing, therefore, is an insurance policy against what is called "bracket creep." A fancy name for the kind of tax increases that many politicians find irresistable: the ones that slip in through the back door. But, even more importantly --and I can't stress this too strongly-- indexation is an insurance policy against inflation.

If politicians can get more tax dollars to spend by means of inflation, the temptation will be to favor inflation. Oh, not a lot, just a little flirtation here and a little flirtation there. Unfortunately, flirtations have a way of getting out of hand. And flirting with inflation is like flirting with fire--it's hard to control and it can burn your house down.

I put so much stress on indexing because it is so very important, and because there is now an effort gaining some steam in the House of Representatives, to repeal indexation. The reason given is bad enough--which is to raise your taxes. And that it would certainly do, by an estimated $98 billion dollars between 1985 and 1988. That's back to business as usual--bad business as usual.

But what is far worse, particularly to older Americans who have the most to lose, is that it would actually reward government policies that produce inflation. Who could possibly expect the big spenders, responsible for our past and present economic problems--responsible, let's face it, for the threat to Social Security--to refrain from spending your good money on the basis of their good intentions, and then setting off the whole inflationary spiral once again?

A wise man once said those who don't learn from history are bound to repeat it. Well, history has certainly taught us that inflation is dynamite, and politicians will play with that dynamite if they can get away with it. That is why I urge this audience, which certainly has learned from history, not to let the politicians repeal this all important guarantee against inflation and re-inflation.

If there is some misunderstanding about indexing, then indexing is clarity personified compared with another aspect of tax law--the withholding of a limited amount of taxes on interest and dividend income. But while the misunderstanding about indexing arises from the novelty of government actually trying to curtail inflation, the misunderstanding about withholding stems from a clever, well financed campaign, not to clarify, but to obscure, to mislead and to frighten.

They say that while a lie goes speeding around the world, the truth is often still fumbling to get on its walking shoes. Well, I've got my shoes on and I want to offer some straight talk about the withholding provision of the 1982 tax law.

First, it is not a new tax. There has always been a requirement to pay taxes on interest and dividends. Unfortunately, a great many people have neglected their responsibility to do so, thereby placing an unnecessary burden on other taxpayers, including those who don't have any income in the form of interest and dividends.

Second, the withholding provision has been carefully designed to make sure it works no hardship on anyone, and particularly retired persons. Thus, for those over 65, withholding will apply only where the individual has income -- over and above social security -- of $14,450, and on a joint return income over $24,214. As a result, over 85 percent of retired persons are exempt from withholding.

Third, and finally, IRS expects the withholding provision to produce some $26 billion in tax revenues through 1988, again, not in new taxes, but in taxes not now being paid. At a time when government is hard pressed to meet its obligations for Social Security and other vital purposes, if it were not for the withholding provision, it would be necessary to institute some other tax, which might very well affect retired persons infinitely more than the current modest withholding provision.

Since Arthur's invitation asked me to deal with the whole gamut of budget provisions of importance to you, let me mention one other very important, but often overlooked, issue. And this may sound strange coming from a Treasury Secretary, but it has to do with my admonition: Guard your health; it's more valuable than your money.

Perhaps the most important non-fiscal reform in the President's new budget is that for the first time, Medicare beneficiaries will be protected from the devastating cost of catastrophic illnesses involving lengthy hospitalization.

If Congress acts on this provision, as we hope it will, then no longer will older Americans be in danger of having their entire life savings wiped out by some medical catastrophe. I'm talking about the runaway costs of health care, which have been rising at a rate that threatens the capacity of the system to meet future medical claims and needs. Now, as a result of fair and balanced health care financing proposals, everyone--doctors, hospitals, insurers, consumers, employers and government--will at last be working together to control health care costs.

How will this be accomplished? By the same principles offered so long ago by the first Secretary of the Treasury, Alexander Hamilton, when our new nation seemed on the brink of bankruptcy. Hamilton offered President Washington a comprehensive plan based on a principle that recent Administrations lost sight of. That principle was--incentives. If there is one unifying principle underlying everything that President Reagan has sought to achieve it is exactly that: restoring incentives for health care providers, incentives for them to deliver their services more efficiently. We are seeking to get more competition and efficiency into the medical marketplace so that the Medicare element of Social Security can continue to meet its obligations.

Let me conclude by contrasting two approaches to government. One is the government of inadequately examined good intentions that builds a skyscraper of promises on shifting sand. The other government understands that in the real world good intentions alone are insufficient and, ultimately, a danger both to those who offer them and those who believe them. This government seeks to build on solid ground.

The winds of time and circumstance can flatten structures built on sand. And that is what we have all been suffering through these last few years. But now we are building on a firm foundation and the walls are going up.

Now that we have together repaired the damages of neglect and foolishness, don't--not for my sake, not for the sake of any President or any Administration, but for your sake and the sake of all older Americans -- don't let the fast talkers and great promisers turn us back to where government went wrong.

Thank you.

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TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

Testimony
by
Charles Schotta
Deputy Assistant Secretary
for
Arabian Peninsula Affairs
before the
House Committee on Government Operations,
Subcommitte on Environment, Energy, and Natural Resources

March 16, 1983

Mr. Chairman and distinguished members of the Subcommittee:

I welcome this opportunity to present the Department of Treasury's views on the major potential economic and financial implications of recent developments in the world oil market.

During the past several months, continual softening of the oil market raised questions about the gains or losses that would result from a fall in world oil prices. The continuing disarray within OPEC added fuel to discussion of these questions. Some observers expressed unqualified enthusiasm at the prospect of reductions in oil prices, believing that they would lead to higher economic growth, lower unemployment and lower inflation in the U.S., the other OECD countries, and the oil importing LDCs. In addition, their current accounts and, in particular, the debt problems of most LDCs would be improved. Others have been less sanguine, noting that oil-exporting LDCs -- including some of the most worrisome cases -- would be hurt, and that international financial problems would be exacerbated. Some also feared that lower oil prices would mean that gains in

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energy conservation could be slowed, reduced oil exploration and development could be expected, and losses in specific energy sectors would ensue.

Granted that a mixture of positive and negative effects will follow the oil price decline, where do we come out on all this? The Administration believes that the decline in oil prices which has been agreed by OPEC is clearly to be welcomed, with beneficial net effects. It will contribute toward economic recovery in the industrialized and developing oil importing countries and reduce inflationary pressures. While problems may arise during the transition to lower oil prices, the U.S. Government will carefully monitor the situation.

In this connection,I should like to point out that the policy of the Administration in energy matters, as in other areas, has been to rely on market forces, for example, decontrolling oil prices in January, 1981. This policy has worked well.

Let me review in greater detail some of the effects which should accompany an oil price decline. Unless otherwise noted, the economic effects that I will discuss are predicated on a hypothetical 20 percent fall in oil prices from an average of about $33/bbl to an average of $26-$27/bbl. I have used 20 percent as a rough unit of measurement for whatever does happen to oil prices. Generally speaking, however, a price reduction of 2/3 as much -- to roughly $28.50/bbl, which is our initial estimate of the effect of the recent OPEC decision -- would produce about 2/3ths of the effects discussed.

Let me emphasize that I am not forecasting that oil prices will decline to $26/bbl. The price, of course, will be determined by the market. Let me also emphasize that our estimates of the economic impact of this hypothetical oil price decrease are based on a large number of assumptions, involve a great deal of uncertainty, and should be viewed as tentative.

EFFECTS ON THE U. S. ECONOMY

Looking first solely at the U. S. economy, there would be multiple effects of $26 oil.

-- Transfer effects. There would be significant redistribution -- or transfer -- effects among various groups. In 1982 the United States spent about $173 billion on 5.55 billion barrels of oil. Of that, 3.9 billion barrels were produced domestically, and 1.6 billion barrels imported. A 20% price cut would lower our total oil bill by slightly more than $36 billion per year. Approximately $10 billion of this would be a transfer of income from foreign sellers of oil to American consumers, amounting to roughly 0.4 percent of GNP. About $26 billion would be shifted from U.S. oil producers, and from governments which levy taxes on oil, to U.S. oil consumers. Thus, there would be some losers in this situation, but the nation as a whole would be better off.

-- Output, Price and Employment Effects. This would stimulate an expansion in aggregate output and employment. It would be the reverse of the so-called "oil drag" that occurred as a result of oil price increases in the 1970's. All told, it would not be unreasonable to assume that the level of U.S. real GNP would be about 1/2-3/4 percentage points higher than would otherwise have been the case within a year or two after a 20 percent drop in world oil prices.

The direct effect on the GNP deflator would be a drop of roughly 1/2 to 3/4 of a percent. The impact on the CPI would be about 50 percent greater because of the large weight of petroleum products in the CPI, and because the CPI reflects the price of oil and energy products produced abroad and imported into this country. In addition, lower oil prices would affect the costs of producing other goods and services, (virtually all products incorporate some oil, if only in their transportation) and there would be secondary effects through escalator clauses, etc.

-- Current Account. The oil import bill would drop by about $10 billion. However, this effect (plus an export gain due to higher economic activity in other oil-importing countries) would be partially dissipated by an increased volume of oil imports, increased imports of other goods and services stemming from higher levels of domestic economic activity, and reduced levels of U.S. exports to foreign oil-producing nations. On balance, therefore, we would expect the U.S. current account to benefit by something less than the fall in the oil bill.

-- Sectoral Impacts. Reduced consumer expenditures on direct energy purchases would leave them with more disposable income to spend on other goods and services, benefiting nearly every sector of the economy. Moreover, a drop in oil prices would put downward pressure on prices of other energy forms. Thus, energy consuming industries would experience reduced production costs which could be reflected in lowered product prices, thereby increasing sales.

The list of industrial and service sectors likely to benefit is extensive, including chemicals and fertilizers, wholesale and retail trade, steel, mining, airlines and aircraft manufacturing, paper mills, agriculture, food processing, trucking and water transportation, and construction. At the same time, coal production could be adversely affected, and the rail sector could encounter reduced coal shipments. The banking sector would experience some problems arising from domestic loan exposure to energy related industry (exploration, drilling, synfuels) as well as international exposure to oil-exporting LDCs. However, higher real economic growth would work to strengthen most borrowers and, therefore, the collateral position of banks.

There would, of course, be negative effects on domestic energy industries. Prices of domestic oil would follow internaational oil, and there would be ripple effects in other energy industries due to price competition. Effects would also vary within the petroleum industry. The heaviest impact would likely be on production-oriented companies and production service companies, in particular companies which have invested in high cost production with heavy reliance on bank financing. On the other hand, downstream operations in refining and marketing might benefit from improved processing margins as demand for petroleum products rises due to lower prices.

EFFECTS ON OECD NATIONS

The OECD countries consume roughly 34 mmb/d -- somewhat more than $400 billion per year at current world prices, and about five percent of aggregate OECD GNP. A 20 percent price cut would reduce this bill by about $80 billion.

The direct effects on aggregate GNP growth would come mainly from a reduction in the cost of OECD oil imports. At current world oil prices, OECD net oil imports -- about 20 mb/d in 1983 -- would cost roughly $240 billion. This bill would fall by almost $50 billion. Exceptions to the OECD experience would be the UK and Norway, which are net exporters of oil. Nevertheless, the net effect on OECD growth and inflation would be roughly in line with that in the U.S.

EFFECTS ON OIL IMPORTING DEVELOPING COUNTRIES (OIDCs)

Oil-importing LDCs would benefit most dramatically from an oil price decrease. They are currently expected to import about 6.6 mmb/d in 1983, costing about $80 billion at current prices. A 20 percent price cut would reduce this by about $16 billion, freeing foreign exchange earnings for additional investment, consumption, or debt service. This alone would increase their aggregate GDP by perhaps a full percentage point. In addition, their exports would increase as a result of increased OECD growth -- giving further stimulus.

It is worth noting that of the ten largest LDC debtors to commercial banks, eight are OIDCs and could be expected to benefit materially from lower oil prices. Brazil, for example, could see its oil import bill drop by perhaps $1-1/2 billion.

OIL EXPORTING DEVELOPING COUNTRIES

Obviously, the big losers from an oil price decline would be the oil exporting LDCs -- the OPEC nations plus a handful of non-OPEC oil exporters. If oil prices were to remain unchanged, the OPEC nations would probably have experienced a small collective 1983 deficit on current account.

With a 20 percent cut, OPEC oil export revenues would be more than $40 billion lower in the first full year following such a price decline and revenues of the four major non-OPEC oil exporters (Mexico, Egypt, Peru and Malaysia) would be lower by $5-6 billion.

As for the Arab Gulf OPEC producers, about which fears have been raised regarding potential disruptive effects on their investment flows, a 20 percent price cut would probably result in only a minor collective acount deficit.

EFFECTS ON THE INTERNATIONAL FINANCIAL SYSTEM

Finally, let me conclude by commenting on the effect of the international financial system.

It is generally accepted that the overall quality of banks' international loan portfolios would improve, reflecting the generally improved position of non-oil LDCs, but loans to some large borrowers heavily dependent on oil exports might become more vulnerable to delays and interruptions in payments. Indonesia, Mexico, and Venezuela are most frequently mentioned in this regard.

We have, however, reviewed the situation and concluded that the U.S. banking system and the international financial system could withstand very serious problems on their loans to the oil producers -- problems far more serious than anything that has occurred or is likely to occur. Thus, for example, even if U.S. banks were not to receive any payment on their loans to Mexico for a protracted period of time -- in our judgement a highly unlikely outcome -- their profits would be hurt, but not destroyed. The improvement in the world economic outlook which an oil price decline would produce would tend, however, to provide offsetting gains for Mexico and other oil-exporting debtor countries.

Summary

To summarize our assessment of the effects of a decline in world oil prices, let me reiterate the following points:

-- A decline in oil prices would clearly be welcome.

-- It would contribute toward economic recovery in the industrialized and developing oil importing countries.

-- The debt servicing problems of oil importing developing countries would be eased, as a result of both lower oil bills and improved export prospects.

-- Some oil exporters would experience declines in revenue, which could create new, or intensify existing, problems.

-- While these, and other such problems, will require careful attention, they do not present a threat to the world trading or financial system.

-- The appropriate departments of the U.S. Government, such as the Treasury, State, Interior, Energy, the Comptroller of the Currency, and the Federal Reserve, are monitoring the situation.

-- Where necessary, the U.S. Government will coordinate with our allies among the industrialized and developing nations to assure an orderly response to oil market changes.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR RELEASE UPON DELIVERY
Expected at 10:00 a.m.
March 15, 1983

STATEMENT OF
ALAN W. GRANWELL
INTERNATIONAL TAX COUNSEL
DEPARTMENT OF THE TREASURY
BEFORE THE PERMANENT SUBCOMMITTEE
ON INVESTIGATIONS OF THE SENATE
COMMITTEE ON GOVERNMENTAL AFFAIRS

Mr. Chairman and Members of the Subcommittee:

I am pleased to appear before you today to provide an overview of some of the initiatives of our tax treaty program to prevent the avoidance and evasion of U.S. income taxes.

The Purpose of Tax Treaties

As background to my discussion, it may be useful to briefly review with you the purposes of income tax treaties. The two primary purposes of bilateral income tax treaties are to mitigate double taxation of income and to provide mutual assistance in combatting tax avoidance and evasion.

With respect to the mitigation of double taxation, income tax treaties divide the taxing jurisdiction between the two countries that are parties to the tax treaty. In general, with respect to a particular item of income, the country in which the income arises (the source country) is required by the treaty to reduce or eliminate its tax in favor of tax by the country of residence of the recipient. In return, the country of which the taxpayer is a resident is obligated to relieve double taxation, to the extent that a tax is imposed in the source country, by allowing a credit for the source country tax or exempting the income from its tax, as the case may be.

In the normal treaty relationship there are flows of income in both directions; therefore each country will cede all or a portion of its right to tax certain income from sources in its country and each country will provide relief with respect to income of its residents from sources in the other country. In that regard, income tax treaties generally provide for reduced rates of tax at source on investment income (dividends, interest and royalties) by the host country so that the aggregate tax burden on the investor will not exceed that which he would pay if he invested at home.

With respect to exchange of information, tax treaties provide elaborate mechanisms for each contracting state to, among other things, obtain tax-related information with respect to their residents and other taxpayers and consult with the tax authorities of the other state on measures to prevent the avoidance and evasion of taxes.

Treaty Shopping

One treaty abuse that the United States is trying to control is treaty shopping. Treaty shopping, in essence, is the ability of residents of countries other than the countries that are parties to the treaty to derive treaty benefits, such as rate reductions on passive income, by channelling investments through entities organized in, or resident in, a treaty jurisdiction. Treaty shopping results in tax avoidance because treaty benefits are obtained by unintended beneficiaries. This weakens our ability to expand our treaty network and to successfully renegotiate more favorable provisions in our existing treaties. Thus, if residents of countries with which the United States has no treaty can avail themselves of U.S. treaty benefits, their countries of residence may have little incentive to enter into treaties with the United States. Similarly, if residents of countries which have a tax treaty with the United States can obtain greater benefits by treaty shopping, in cases where U.S. residents cannot obtain reciprocal benefits, their countries of residence are under little or no pressure to renegotiate their treaties to address U.S. concerns.

It is established U.S. tax treaty policy to include a limitation of benefits article to prevent treaty shopping. These provisions act to, among other things, deny treaty benefits in appropriate circumstances and thereby permit the United States to impose its full statutory rate of tax on payments to such interposed entities. Limitation of benefits provisions will be employed wherever necessary, and in the form appropriate to the circumstances, to assure that U.S. policy goals are served by the extension of benefits in our tax treaties.

Re-examination of Tax Treaty Compliance

Under present law, a recipient of U.S. source dividends who has an address in a country with which the United States has a tax treaty which provides for a rate reduction with respect to such income will, with limited exceptions, be presumed to be a resident of such country for purpose of obtaining reduced rates of tax on such dividends. With respect to interest and other types of passive income, a foreign taxpayer may obtain a rate reduction by certifying his eligibility for treaty benefits to the withholding agent.

Both of these methods of obtaining reduced rates of tax under a treaty are subject to abuse. The address system of withholding of tax on U.S. source dividends is particularly vulnerable since such system permits tax evasion by persons who are not legitimate treaty beneficiaries but who merely establish post office boxes or nominee accounts in countries with which we have a tax treaty providing for reduced rates of tax on dividends. The only real check on this abuse is provided by certain of our treaty partners who collect and remit additional taxes to the United States if they determine that a particular dividend recipient is not a bona fide treaty beneficiary. However, much abuse goes undiscovered and, even with respect to amounts remitted by our treaty partners, substantial costs in terms of delay and uncollected interest are inevitably incurred. The self-certification procedure which applies to interest and other types of passive income is similarly subject to abuse in that it requires a person claiming treaty benefits merely to submit an unverified, self-serving statement to a withholding agent, who is entitled to rely on such statement for purposes of reducing the amount of tax withheld. The Treasury Department detailed its concerns with respect to these procedures in testimony at hearings held on June 10, 1982 before the Subcommittee on Commerce, Consumer, and Monetary Affairs of the House Government Operations Committee (the "1982 Hearings").

Section 342 of the Tax Equity and Fiscal Responsibility Act of 1982 ("TEFRA") was enacted in response to the concerns raised at the 1982 Hearings. Section 342 directs that procedures be designed which will prevent the kind of abuse that occurs through the improper use of nominees and other conduits that pass U.S. source income through to a person who is not a bona fide resident of the treaty country.

A number of alternatives to the present enforcement system exist, including the adoption of a refund system of withholding tax on passive income. A refund system would require withholding agents to withhold U.S. tax at the statutory 30-percent rate on all U.S. source passive income paid to foreign persons, regardless of the potential application of a treaty provision reducing the 30-percent rate or eliminating the tax altogether. The foreign recipient who claims treaty benefits would then be required to file a claim for a refund on an annual tax return. Supportive documentation would be required. Another approach, the "certification system," would require the foreign recipient to file a certificate of residence from the competent authority of the country whose treaty benefits are being sought. Pursuant to the mandate of section 342, we are presently considering such stricter procedures.

Exchange of Information

It is an established principle of international law that a country is not obliged to assist in the enforcement of the penal or tax laws of another country in the absence of an applicable treaty or bilateral agreement. Different types of international agreements may be used by the United States as a basis for obtaining information about foreign activities of U.S. taxpayers, including bilateral income tax treaties, bilateral mutual assistance treaties, and exchange of information agreements.

Exchange of Information Under Income Tax Treaties

Tax Treaty Provisions. Each of our income tax treaties contains a provision requiring the exchange of tax information. The scope of these provisions varies considerably.

Our 1981 draft model income tax treaty ("1981 Model"), which serves as our opening position in treaty negotiations, contains very broad information exchange provisions. It extends to any information necessary for carrying out the provisions of the treaty or the domestic laws of the contracting states concerning taxes covered by the treaty insofar as the taxation thereunder is not contrary to the treaty. The 1981 Model also provides that, for purposes of information exchange, the taxes covered by the treaty are deemed to be all taxes imposed by a contracting state at a national level, thereby including taxes other than income taxes covered by the treaty. The broader information exchange provisions of the 1981 Model have been included in our recently ratified treaties.

Because exchange of information provisions cannot be totally expansive, the 1981 Model includes certain limitations on the obligations of the parties to gather or exchange information. There is a provision expressly limiting obtainable information to that available under the laws of the requested state. In addition, a requested state is typically not required (1) to carry out administrative measures at variance with its laws and administrative practice or those of the requesting state; (2) to supply information not obtainable under the laws or in the normal course of the administration of either state; or (3) to supply information which would disclose any trade, business, industrial, commercial, or professional secret or trade process, or any information the disclosure of which would be contrary to public policy.

The information exchange provisions in the 1981 Model also contain limitations on the use of information exchanged. Information exchanged must be subject to the same taxpayer protections of secrecy as tax information normally receives in the requesting state. The information may in any event only be disclosed to persons involved in the assessment, collection or administration of the tax laws of the other country. In that regard, the Treasury has made special efforts to ensure access by the General Accounting Office to information received under tax treaties. The 1981 Model also provides that information may be disclosed in public court proceedings or decisions.

Kinds of Information Exchange Employed by the United States Under Tax Treaties. The United States generally engages in three methods of information exchange under current tax treaty provisions:

(i) routine or automatic exchanges, consisting primarily of the exchange of names of taxpayers and the amounts of passive income they receive from sources within the other contracting state;

(ii) exchanges of information on the specific request of one of the contracting states;

(iii) spontaneous exchanges of information, transmitted at the discretion of the transmitting country, when information comes to its attention which suggests or establishes noncompliance with the tax law of the other contracting state.

In addition, the Internal Revenue Service has executed simultaneous examination agreements with five treaty partners. These agreements provide for simultaneous examination of multinational corporations in carefully selected cases. Generally, these examinations are of multinational corporations engaged in tax haven operations.

The program has been successful and the Internal Revenue Service is in the process of extending it to other treaty partners.

The Internal Revenue Service has also undertaken industrywide exchanges of information with treaty partners. The objective of these exchanges is to secure comprehensive data on worldwide industry practices in such industries as oil and gas and pharmaceuticals.

The United States is continually striving to develop new and improved methods to cooperate in information exchange with our tax treaty partners to combat international tax avoidance and evasion.

Mutual Assistance Treaties

The United States is also engaged in negotiating mutual assistance treaties in criminal matters. I will leave discussion of these treaties to my colleagues from the Justice Department.

Exchange of Information Agreements and the Caribbean Basin Initiative

There are countries which do not have an income tax treaty with the United States, either because agreement on terms is not possible or because they do not have income taxes, but with whom it may be possible, in certain circumstances, to negotiate a more limited agreement to exchange information. This approach has been proposed in the Caribbean Basin Initiative ("CBI") legislation, which requires an exchange of information agreement as a condition precedent for the extension of certain U.S. tax benefits relating to tax deductions for foreign conventions held in a qualifying CBI country.

More specifically, the CBI legislation authorizes the Secretary of the Treasury to negotiate and conclude the exchange of information agreements. While the Secretary is accorded discretion regarding the kinds of information to be included within the scope of the exchange of information provisions, the legislation imposes certain minimum standards for such agreements. The exchange of information provisions in the agreements must include within their scope tax information (both civil and criminal) pertaining to U.S. taxpayers, residents of the CBI country and "third-country persons," that is, nationals or residents of countries other than the United States or the CBI country that is a party to the agreement. This approach is consistent with our present tax treaty policy, embodied in our 1981 Model. Thus, a jurisdiction with restrictions on disclosure of information regarding such third country persons or having financial secrecy laws would have to modify such laws to enter into such agreements and obtain the tax benefits of the CBI.

Conclusion

The approaches I have described are an important part of the initiatives undertaken by the United States to combat international tax avoidance and evasion.

I thank you Mr. Chairman and members of the Subcommittee for your interest in the matters which we have addressed today and am pleased to have had the opportunity to consider these important issues with you.

I would be happy to entertain any questions you might have at this time.

March 14, 1983

OPEC

STATEMENT BY SECRETARY REGAN ON OPEN DECISION

The OPEC decision reached today in London is clearly good news for the United States and for the world economy. It will mean less inflation and will serve as a strong shot in the arm to the budding economic recovery.

The oil price reduction will obviously place some strains on certain oil exporters with large external debts. However, of the 10 nations with the largest debts, 8 are oil importers. This action will be of great benefit to them as well as to the other less developed countries.

The shift of the "official price" of OPEC oil down to $29 a barrel is much more in line with the already prevailing market prices. In spite of what many might think, the price of oil -- like other prices -- is ultimately determined by supply and demand. And it will be interesting to see if the production quotas that OPEC agreed to will be sufficient to maintain this newly agreed to price level.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

For Release Upon Delivery
Expected at 9:30 a.m.
Thursday, March 17, 1983

STATEMENT OF MANUEL H. JOHNSON
ASSISTANT SECRETARY FOR ECONOMIC POLICY
BEFORE THE
SUBCOMMITTEE ON CONSUMER AFFAIRS
OF THE
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE WASHINGTON, D.C.

Introduction

It is a pleasure to be with you today to inquire into the reasons why interest rates in general, and those paid by consumers in particular, have remained at relatively high levels. It seems to me that high interest rates -- in both nominal and real terms -- are a direct consequence of the way that the economy has performed for a decade or more and the policies that have been followed. Therefore, my statement today deals mainly with the broad economic forces which have determined the general level of interest rates.

Some attention is also given in my statement to possible factors influencing relationships within the structure of interest rates. This structure ranges from the rates on Treasury obligations, which are free of default risk and hence provide a sort of base line, up to the much higher rates that prevail on credit card balances of individual borrowers and unsecured personal loans. Others who are appearing before your Committee, however, will be better able to discuss the specific features of different types of loans, the cost structure of lending institutions, the pattern of financial practices and other such matters that are understandably of concern to your Committee. Most of my attention will be directed to the general economic background.

R-2091

Interest Rates and the Economy

Nominal interest rates are down sharply from their peak levels but they remain high by historical standards. For example, the 3-month Treasury bill has recently been trading around 8-1/4 percent on a bank discount basis, less than one-half of its late 1980 peak of 17.14 percent, and down about 4 percentage points since last summer. The commercial bank prime lending rate is currently at 10-1/2 percent, less than one-half of the 21-1/2 percent peak first reached in late 1980 and down 6 percentage points since last summer. The economy is still in the early stages of cyclical recovery and interest rates can still decline somewhat further but that depends primarily upon our making continued progress against inflation, achieving moderate rates of monetary growth and reducing financial risk in general.

Inflation already experienced over the past 15 years and feared in the future is the fundamental reason for high nominal interest rates. Rising rates of inflation after the mid-1960's led to a roughly parallel rise in key interest rates. Chart I, attached to my prepared statement, shows a close relationship over the period between the 3-month Treasury bill rate and the annual rate of inflation. Sustained periods of monetary over-expansion drive up the rate of inflation and pull up the entire structure of interest rates. That is what occurred following the mid-1960's.

The relationship between inflation and nominal interest rates is relatively simple. Lenders will require, and borrowers are willing to pay, something for the use of funds. But lenders find that something turns to nothing when inflation begins to exceed the rate of interest at which they lend. Their reluctance to lend at a loss and the continuing demand of borrowers gives rise to market forces that operate over time to build a premium into the interest rate structure which is equal to and offsets the expected rate of inflation, leaving lenders with the prospect of some positive real return.

As may be seen in Chart I, the 3-month Treasury bill rate exceeded the inflation rate consistently throughout much of the 1960's. Some positive real rate of interest has been generally characteristic of financial experience in this country -- a real rate of 2 percent or so is often taken as typical. By the mid-1970's a new relationship was emerging with inflation exceeding interest rates and real rates of interest driven to negative values. Such a situation was possible since the Federal Reserve was holding down interest rates by more rapid monetary expansion than expected by investors. The danger of the policy became increasingly clear as inflation threatened to run out of control, and in October 1979 the Federal Reserve announced a new approach to the conduct of monetary policy that placed greater emphasis upon control of the monetary aggregates. Since this change in Fed policy, inflation has come down but interest rates have remained relatively high, resulting in very high real rates of interest. This shows up as a wide differential since 1979 between the two series in Chart I.

The persistence of high real interest rates is something of a puzzle. Certainly it is not an issue that can be settled today, or perhaps in the foreseeable future. Disagreement among economists on such issues is notorious. One can only suggest some major influences.

It should be emphasized that the negative real interest rates of the late 1970's were a departure from normal. The strength and persistence of inflation was clearly underestimated in financial markets thereby temporarily reducing the realized real rate of return below zero. Expectations of future inflation were undoubtedly strengthened during these years. This has subsequently been reflected in the much higher real interest rates of recent years which can be viewed as a market reaction to the earlier subnormal returns. In this context, it is important to note that real interest rates will not seem so high currently to the long-term supplier of funds who envisages an eventual return to double-digit rates of inflation. This illustrates the important point that in the case of long-term interest rates, the damage done by a sustained period of inflation cannot be repaired quickly. But, if low rates of inflation continue, both real and nominal interest rates will eventually show further declines.

Another factor contributing to the persistently high level of real interest rates is that the period since October 1979 has been one of much greater volatility in monetary growth and interest rates. The shift by the Federal Reserve to increased emphasis on the monetary aggregates was essential. In the broadest sense, the change in policy may be responsible for much of the progress that has been made against inflation. But the implementation of that policy -- as perhaps with all policies conceived in this town -- was less than ideal, and resulted in wide swings in money growth. Research at the Treasury Department suggests that the variabilility of money growth has added 2 to 3 percentage points to the level of interest rates over the last two years. Factors other than the volatility of monetary growth such as extreme swings in interest rates and general uncertainty over the financial future may also have contributed to the appearance of higher risk and uncertainty premia in the interest rate structure.

While interest rates are generally regarded as being excessively high there may be some question whether real interest rates are always as high as they seem. Rates which seem excessively high on a pre-tax basis are not quite so striking after tax. In the simplest possible terms, an 8 percent nominal rate of interest at a time of 4 percent inflation yields an investor in the 50 percent marginal tax bracket no after-tax real rate of return whatsoever.

From the standpoint of the consumer-borrower, after-tax real costs are somewhat higher, but chiefly because consumer borrowing costs include an allowance for risk, not present in the case of Treasury securities. For consumers, interest costs are only recently beginning to turn positive. A median income worker, for instance, whose Federal and State income tax would put him in about the 30 percent marginal tax bracket, would have had an after-tax real interest cost of about zero on a 12.9 percent, three-year car loan taken out in late 1979. (This assumes the loan is repaid over the three years ending in the fourth quarter of 1982.) Auto loans taken out in the fourth quarter of last year presumably will result in a positive real interest cost, although that will depend on what the inflation rate is for the next three years. Assuming inflation stabilizes in the 4-1/2 percent area as we are forecasting, real after-tax interest cost would be in the 6-1/2 percent range on 16 percent bank loans and in the 4-1/2 percent range for 12.8 percent finance company loans.

Other explanations, some of considerable complexity, have been advanced as to the current height of real interest rates. That will probably continue to be the case as long as the phenomenon persists. Real interest rates are never directly observable, since they are the difference between nominal interest rates -- which are observable -- and <u>expected</u> rates of inflation which are not. In the final analysis, however, for both real and nominal interest rates, the chief explanation of the difference between the low interest rates of the early 1960's and the high interest rates of the early 1980's is the fact of an intervening era of inflation without parallel in previous U.S. experience. In terms of aggregate economic policy, the most effective way to achieve generally lower rates of interest in the current situation is to achieve consistently lower rates of inflation.

In addition to controlling inflation, it will be very important to offer adequate incentives for saving. Real interest rates are determined by the interaction of the supply and demand for loanable funds. More fundamentally, these supplies and demands reflect the complex of motives and incentives which govern decisions to save along with the rate of return that can be achieved through capital investment. Other things being equal, policies that increase the supply of savings -- such as our incentive-oriented tax reductions -- will help to reduce real rates of interest.

Interest Rates and the Consumer

Over time, then, the general level of interest rates is determined by fundamental economic forces. These include the overall state of the economy, the resultant opportunities for profitable employment of investible funds, the savings rate, which provides those funds, and the outlook for inflation.

At any particular point in time, however, interest rates for alternative investments may differ considerably, with the differences primarily reflecting the riskiness of the investment or loan. The risk may have a number of dimensions, but the major element is the creditworthiness of the borrower, including the possibility of default on the loan or the difficulty that might be experienced by the lender should he need to liquidate it.

Chart II shows the structure of some typical consumer loan rates as they relate to the rate for three-year Treasury notes, a roughly similar maturity. Some measure of the cost of funds to the lender, such as the CD rate, might have been chosen; but the concentration here will be on what might be termed the opportunity cost of lending since detailed and reliable information on the direct cost of lending was not available to us.

Consumer loan rates are generally considered to be administered rates. That is, they are posted by lenders rather than set by the market interaction of supply and demand conditions, such as those on Treasury securities, corporate bonds, and the like. Still, even posted consumer rates must fundamentally reflect competitive forces, especially among lending institutions. (It might be noted that there is substantial regional variation in rates, reflecting local demand conditions.) Total debt owed by households is roughly as large as that owed by nonfinancial business -- each accounting for about 35 percent of total credit market debt owed by the domestic nonfinancial sectors. As a result, there is considerable competition among banks, credit unions, savings and loan institutions, finance companies, etc., for the consumer loan business. At the end of January, the largest holders of the more than $340 billion of consumer installment credit outstanding were commercial banks with 44 percent of the total, finance companies with 28 percent, and credit unions with 14 percent.

While competition may be expected to benefit the consumer by keeping loan rates low, a number of factors cause these interest rates to be higher than those for other types of loans. Others that are testifying before your Committee will be in a better position to discuss the exact mechanism by which the rates are set, but it may be nonetheless worthwhile to review briefly some of the influences that affect these rates.

One of the pressures pushing consumer loan rates up is the small size of the transactions. Outside of mortgage debt, probably the largest transaction for which consumers use credit is automobile purchase, which accounted for over a third of all installment loans outstanding at the end of January. Figures available from finance companies show the average amount financed on a new car purchase is about $8,500. On used cars the amount of the loan is $4,800. For personal loans the average loan size drops to $2,500 and for other consumer goods to less than $1,000. Clearly these loan sizes are much smaller than what could be expected for business borrowing and consequently, the relatively fixed cost of servicing each loan is spread over a small earnings base.

Another factor accounting for the relatively high rates on consumer loans is the greater average risk of default compared, say, to that applicable to a prime business borrower. This relationship varies over time depending on economic conditions. Some analysts feel that in addition to the general risk inherent in the consumer market, the Bankruptcy Reform Act of 1978, which became effective in October 1979, generated added risk to lenders. The new legislation made bankruptcy more palatable in some cases by liberalizing exemptions in the assets that must be turned over to creditors. Personal bankruptcies began to rise sharply thereafter -- doubling between 1979 and 1981. While bankruptcies edged down 1-1/2 percent last year, they are far higher than might be expected on the basis of economic conditions alone, with the 1982 figure 95 percent above the level reached in 1975, the last recession prior to the new bankruptcy legislation. With more consumers seeking relief from debt by declaring bankruptcy, the risk to and burden on lenders has understandably increased.

A further consideration in assessing consumer loans is the term for which they are written. There have been numerous press reports relating the level of consumer interest rates to some of the more commonly publicized rates, such as the prime. In making such comparisons, it should be kept in mind that short-term rates like the prime are inherently much more adjustable to changing market conditions than those issued for longer periods, as is typical of consumer loans. The average term of a new car loan at a finance company was nearly 4 years in 1982; on personal loans maturities were close to 5-1/2 years and on consumer goods about 2-1/2 years. Therefore, it should not be considered unusual that in a transition period from high to low inflation and from high to low interest rates, consumer rates would lag more sensitive borrowing rates until there has been sufficient evidence that the current disinflationary environment is not merely a transitory stage of the economy. Bankers set their rates to include an <u>expected</u> inflation premium and need to be convinced that low inflation rates will continue for the duration of the loan.

With these things in mind, let us take a careful look at Chart II in order to try to evaluate whether recent experience suggests that consumer rates are being held unduly high. The three-year Treasury rate has been used as a base rather than a cost-of-funds measure, such as a CD rate. One reason for this, aside from the fact that the longer term of the Treasury issues is more directly comparable to the term of a large portion of consumer loans, is that recent years have brought some welcome but tumultuous changes in banking. Whereas in the past banks were assured a fairly stable, low cost source of funds through deposits, the introduction of NOW and Super NOW accounts and the new money market deposit accounts has resulted in a scramble to attract and keep deposits by offering high rates of interest on both checking and savings accounts.

Chart II displays a number of key consumer loan rates over the past decade. One obvious point that can be seen from this chart is that consumer rates are not nearly as volatile as other rates. In general the spread between those rates and the risk-free Treasury rate may be assumed largely to represent risk and the added cost of administering those small loans. In each case, the average spread between 1972 and 1977 was higher than in the period from 1978 through 1981. Even though consumer rates began to climb, they did not rise as fast as other rates did. To some extent this lag reflected the impact of state usury ceilings but it was also due to the greater rigidity of consumer loan rates alluded to earlier. Just as consumer loan rates lagged on the way up, they also lag on the way down. As other interest rates began to drop in 1982, the rate structure approached the relationships of the mid-1970's.

- Bank auto loans averaged 3.9 percentage points above three-year Treasuries in the first six years covered by the chart. In the next four years the difference fell to 2.5 percentage points and in 1982 it was restored to 3.9. By the fourth quarter of the year, the difference was a fairly wide 5.8 percentage points. In view of the experience of the previous several years, this should probably not be considered excessive for such a short period of time.

  -- Finance companies, which are largely supported by auto manufacturers, have been taking an increasing share of the auto loan business from commercial banks, clearly reflecting the diminishing profitability of such loans. During 1982 auto manufacturers used loan subsidies as one of the major sales incentives. As a result, the spread between auto rates at finance companies and the three-year Treasuries has fallen steadily from 5.7 percentage points from 1972 through 1977, to 3.3 percentage points in 1978 through 1981 and only 2.9 percentage points in 1982.

In the fourth quarter the difference was a low 2.7 percentage points, reflecting special sales incentive programs sponsored by domestic manufacturers.

- Personal loan rates, like other rates, adjusted higher in the late 1970's and in 1980 and 1981 as inflation worsened. But the pace was slower than the increase in market rates. Thus, the rate spread on 24-month personal loans also dipped from 5.9 percentage points from 1972 through 1977 to 4.2 points in the following four years. Since then, however, the correspondingly more rapid decline in market rates has led to a widening of the personal loan rate spread to the levels of the mid-1970's.

- The spread on credit cards, for which rates have risen only slowly, has fallen continuously from a high 10.1 percentage points in the mid-1970's to 5.6 percentage points in 1982. By the fourth quarter the difference had risen to 8.6 percentage points but was still below its traditional spread of about 10 points.

- Finally, it might be noted that interest rates at finance companies for personal loans and other consumer goods have also shown narrowing of the spreads over the past decade.

Presuming that the period from 1972 through 1977 represented a period in which consumer loan rates were set to grant the lender a reasonable real return, after covering costs of processing and the additional risk associated with consumer loans, it appears that in more recent years the lenders were probably caught in a squeeze that caused consumer loan rates to narrow from their traditional relationships to other rates. During the latter part of 1982 the rate structures began to be restored as market determined rates dropped sharply faster than administered short-term consumer rates. Consequently, spreads for the year as a whole were about back to traditional relationships with other market rates. This statement would also be true if one were speaking about such marginal cost of funds measures as CD's. At various times in 1980 and 1981 the gap between yields on CD's and consumer loans not only narrowed, but CD rates topped those on auto loans and at one point those on 24-month consumer loans. Table 1 and Chart 3 demonstrate more fully rate spreads over the past decade.

Brief comment may be desirable on longer-term consumer borrowing which, in practice, means mortgage borrowing. In the area of long-term finance, market and consumer mortgage rates have moved more closely. In part, this results from the secured nature of the mortgage loan, which accordingly lessens the risk of default loss. In addition, however, the market for mortgages has broadened significantly in recent years through the use of mortgage pools, FNMA activities, and the like. Thus, mortgages have acquired a degree of liquidity that allows their yields to respond to underlying economic forces in a manner more like corporate bond yields. Nevertheless, mortgage rates do tend to respond more sluggishly than other yields, and the spread of the mortgage rate over the long-term Treasury yield is currently slightly wider than has been traditional. (See Charts IV and V which show the levels and spreads between the long-term rates discussed above.)

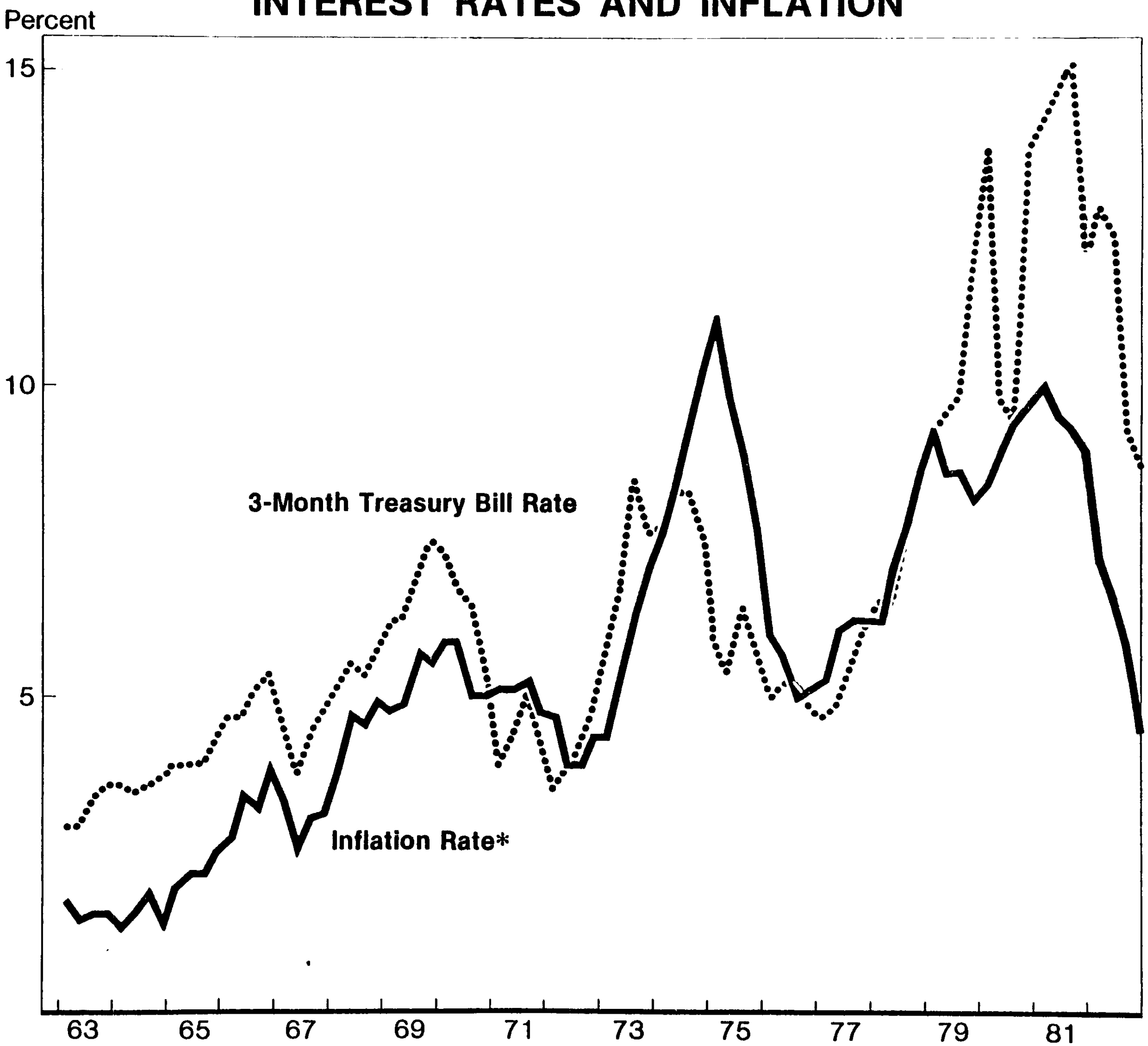
A range of broader influences may also be important in determining the rates that consumers pay at any particular time. For example, the well-publicized losses of U.S. banks on their international lending operations may conceivably be affecting bank pricing decisions on domestic loans. Some latitude probably exists for banks to keep the gross margin on domestic loans wider than normal for brief periods of time. Bank regulators and those closer to actual bank pricing decisions may be in a position to throw some light on this and other similar issues.

Conclusion

In conclusion, there appears to be no readily available evidence that consumer loan rates are somehow being set at levels that are inconsistent with the general economic environment. Stiff competition for the consumer market would prevent this. While fairly wide spreads did develop in the latter part of last year between some consumer and market rates, it is likely that these spreads are at a cyclical peak, reflecting large credit risk assessments, a volatility premium, an expected inflation rate premium substantially larger than the observed rate, and the transition to a new environment in which the average cost of funds may be higher due to deregulation. Presumably as the economy recovers and it becomes clear that inflation and market rates are stabilizing at lower levels or falling further, consumer rates will adjust downward.

In order to ensure that market rates of interest reach more satisfactory levels, we must persevere with efforts to bring inflation down and keep it down. No other single action will do more to ensure the availability of credit to consumers at reasonable rates of interest.

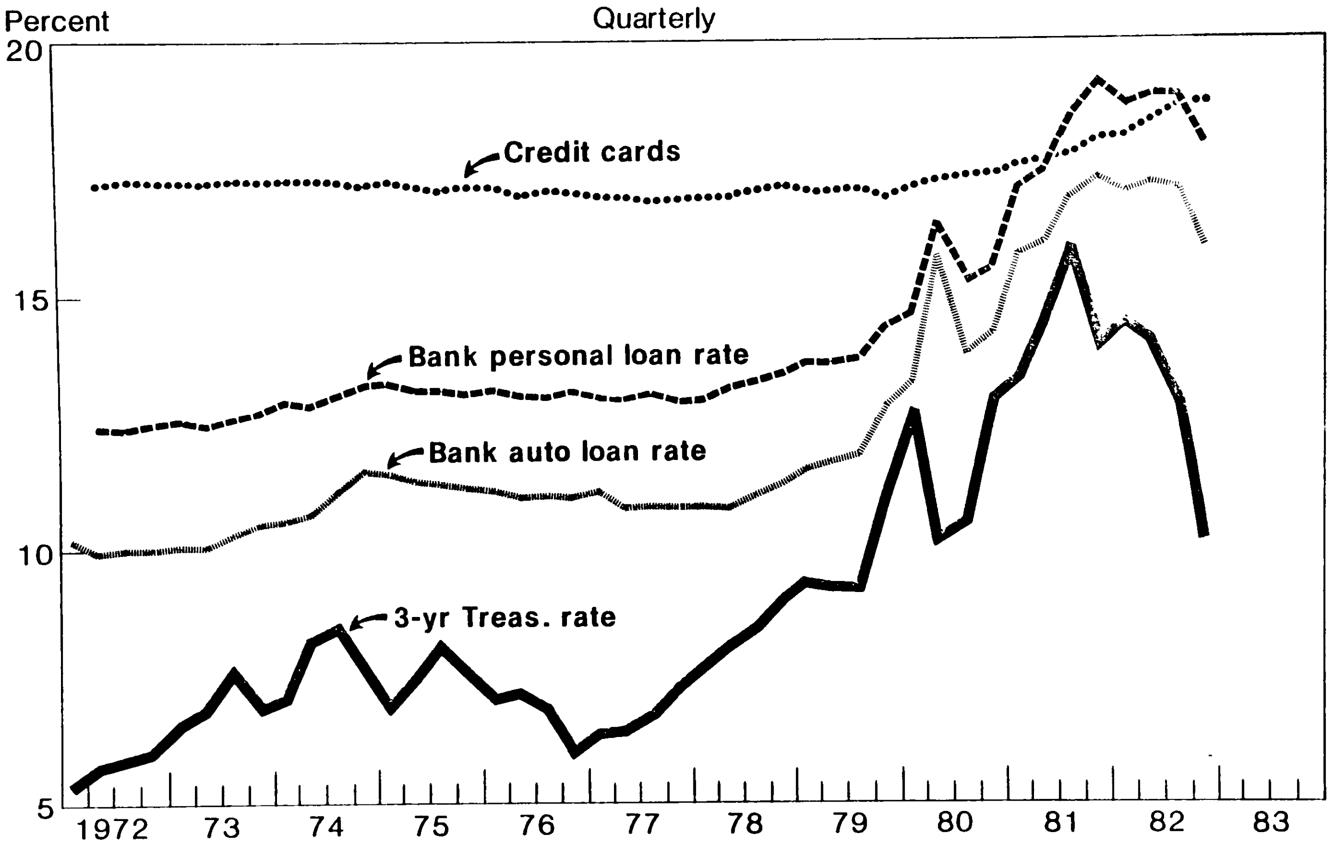
INTEREST RATES AND INFLATION



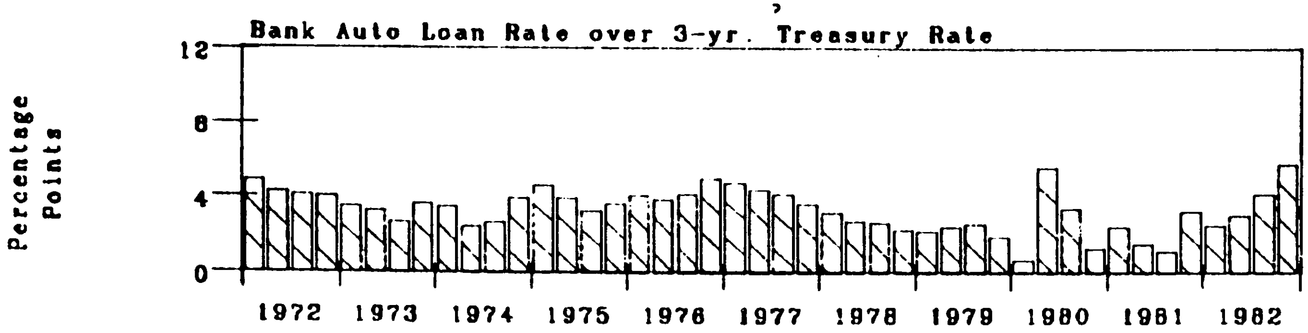
* Growth from year earlier in GNP deflator.
Plotted quarterly.

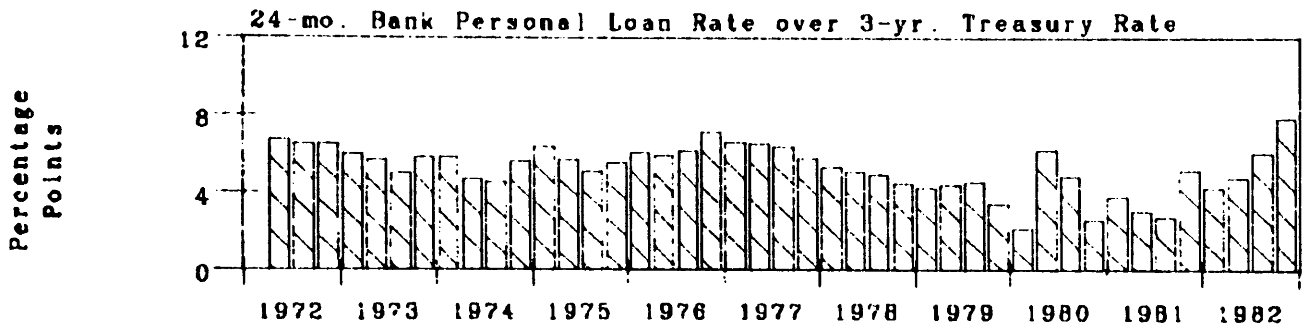
January 19, 1983-A28

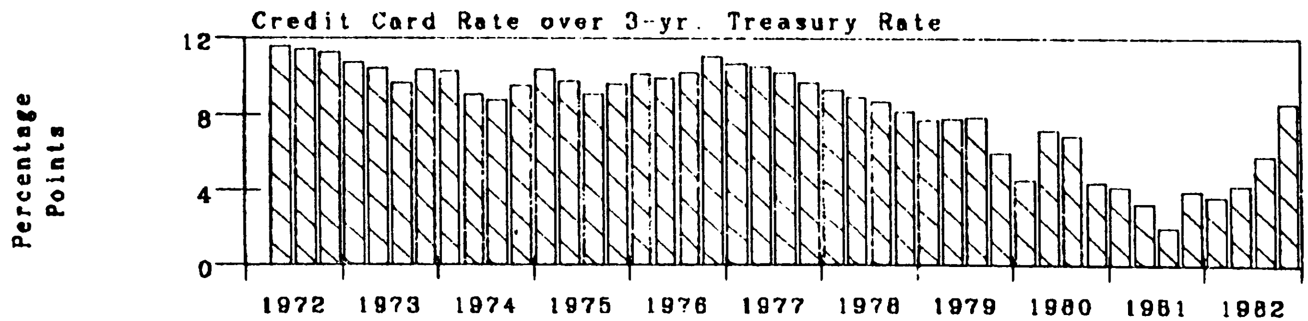
COMPARISON OF 3-YR TREASURY RATE AND SELECTED BORROWING RATES



March 14, 1983 A225

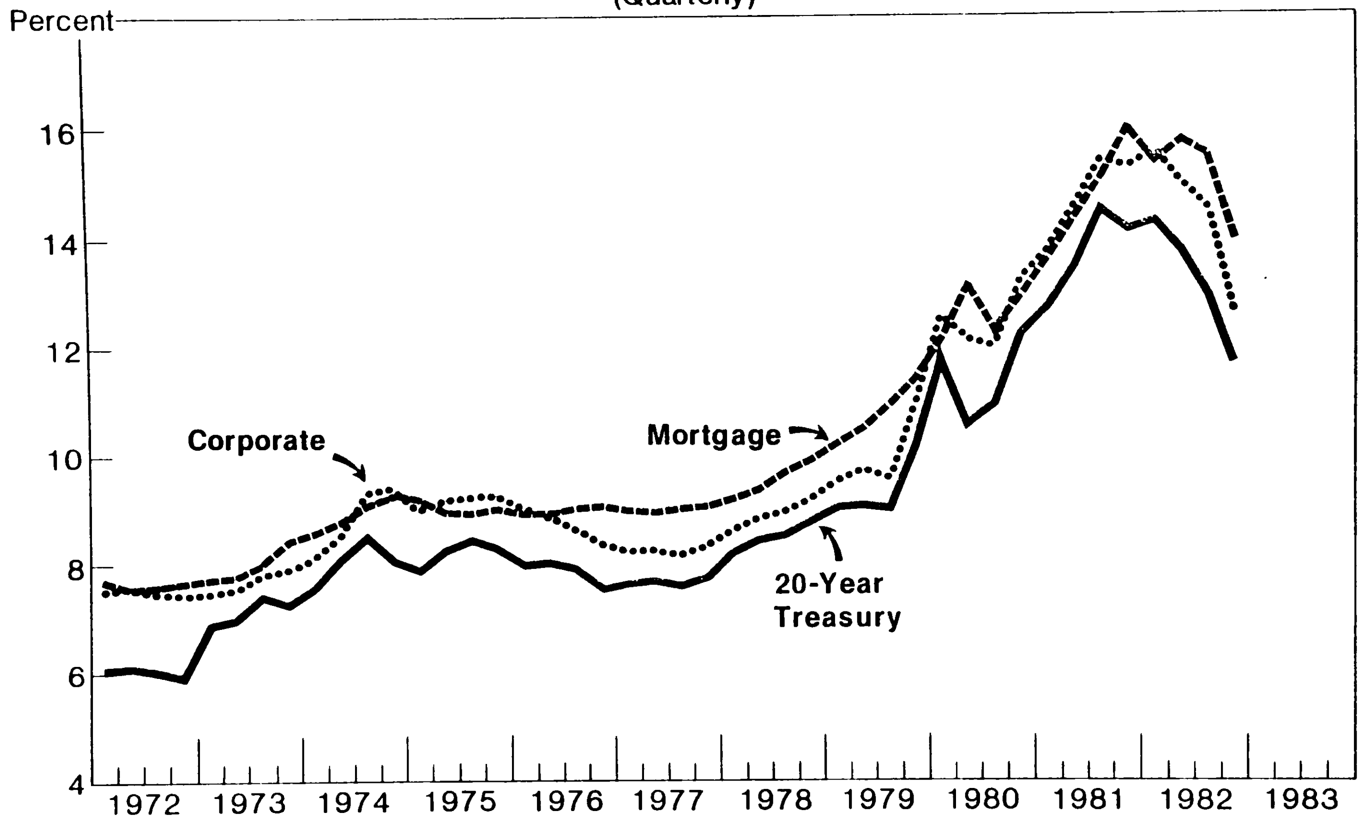

Bank Auto Loan Rate over 3-yr. Treasury Rate
Percentage Points
0
4
8
12
1972
1973
1974
1975
1976
1977
1978
1979
1980
1981
1982


24-mo. Bank Personal Loan Rate over 3-yr. Treasury Rate
Percentage Points
0
4
8
12
1972
1973
1974
1975
1976
1977
1978
1979
1980
1981
1982

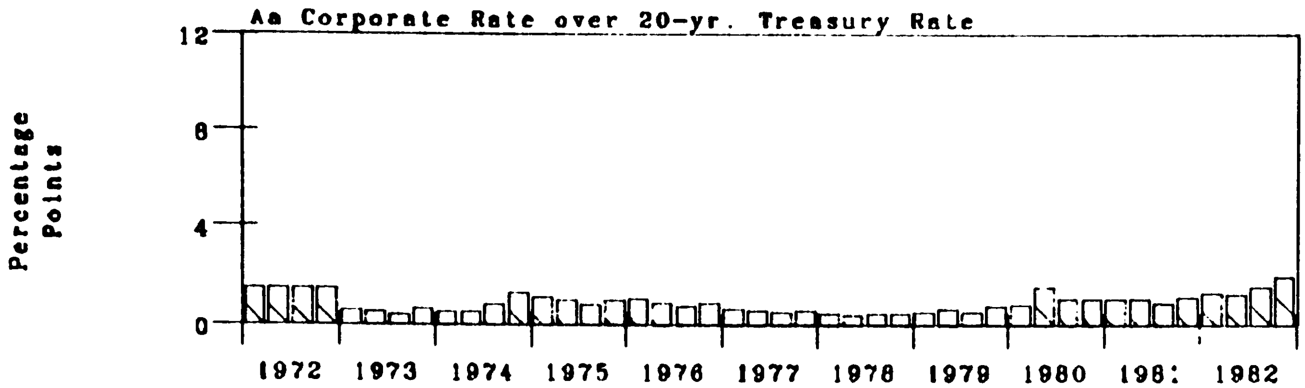

Credit Card Rate over 3-yr. Treasury Rate
Percentage Points
0
4
8
12
1972
1973
1974
1975
1976
1977
1978
1979
1980
1981
1982

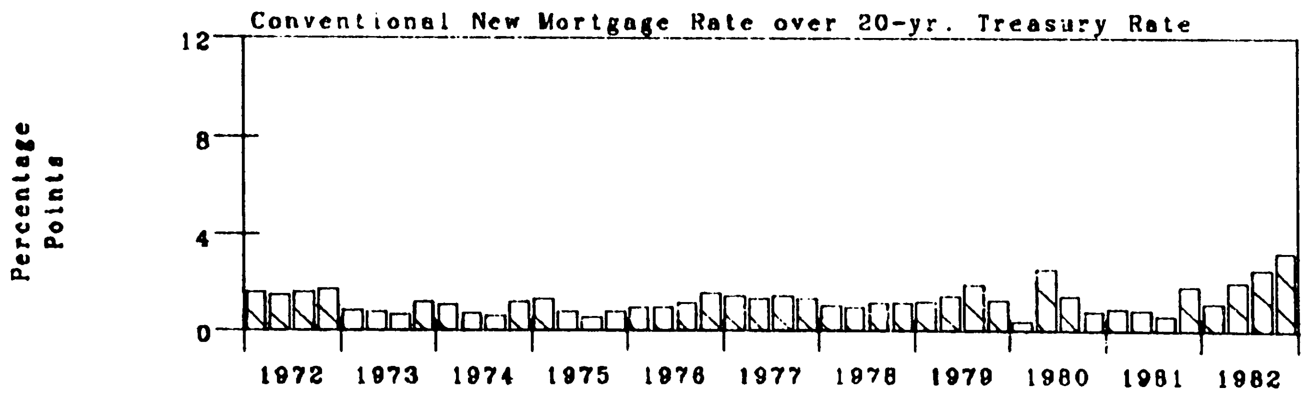
COMPARISON OF 20-YEAR TREASURY, HIGH-GRADE CORPORATE BOND, AND CONVENTIONAL MORTGAGE RATES

(Quarterly)



March 14, 1983 A224


Aa Corporate Rate over 20-yr. Treasury Rate
Percentage Points
0
4
8
12
1972
1973
1974
1975
1976
1977
1978
1979
1980
1982


Conventional New Mortgage Rate over 20-yr. Treasury Rate
Percentage Points
0
4
8
12
1972
1973
1974
1975
1976
1977
1978
1979
1980
1981
1982

Spreads Between Consumer Loan Rates and Other Market Rates of Interest

	Commercial Banks			Finance Companies*		
	Auto loans (36-month)	24-month personal loans	Credit card plans	Auto loans	Personal loans	Consumer goods loans
	Difference from 3-Year Treasuries (percentage points)					
Annual averages						
1972-77	3.9	5.9	10.1	5.7	13.9	12.4
1978-81	2.5	4.2	6.3	3.3	10.0	9.1
1982	3.9	5.7	5.6	2.9	10.2	9.6
Quarterly						
1982: I	2.6	4.3	3.6	3.2	8.4	8.8
II	3.1	4.8	4.3	0.6	8.8	8.6
III	4.2	6.1	5.9	5.0	10.3	9.5
IV	5.8	7.8	8.6	2.7	13.2	11.6
	Difference from 3-Month CD Rate (percentage points)					
Annual averages						
1972-77	4.0	6.1	10.4	5.9	14.1	12.5
1978-81	1.4	3.1	5.2	2.2	8.9	8.0
1982	4.6	6.4	6.2	3.5	10.8	10.3
Quarterly						
1982: I	2.8	4.5	3.9	3.4	8.7	9.1
II	3.0	4.7	4.2	0.5	8.7	8.5
III	5.5	7.3	7.1	6.3	11.6	10.8
IV	6.9	9.0	9.7	3.8	14.3	12.8

* Terms on loans at finance companies generally lengthened over the period.

3/15/83

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE
March 17, 1983

Contact: Charles Powers
566-2041

TREASURY RELEASES FOURTH REPORT ON U.S. CORPORATIONS IN PUERTO RICO

The Treasury Department today released its Fourth Report on The Operation and Effect of the Possessions Corporation System of Taxation. Possessions corporations are companies incorporated in one of the fifty States or District of Columbia that are generally exempt under section 936 of the Internal Revenue Code from Federal tax on their income from Puerto Rico, Guam, and certain other U.S. possessions. These corporations are also generally exempt under industrial tax incentive programs from all or a portion of the otherwise applicable income tax imposed by Puerto Rico and the possessions.

Since over 99 percent of the income of all possessions corporations is derived from Puerto Rico, the body of the report deals with the operation and effect of the possessions corporation system in Puerto Rico.

The principal findings of this report are:

-- The estimated Federal tax savings provided to U.S. corporations under the possessions corporation provisions were $1,156 million in calendar year 1979 and $1,233 million in calendar year 1980.

-- In recent years, one-half of the Federal tax savings have been in the pharmaceutical industry, and one-fifth have been in the electrical equipment and electronics industry.

-- Possessions corporations in manufacturing industries in Puerto Rico employed approximately 72,000 persons in 1980. This represented 9 percent of total employment in Puerto Rico and one-half of all employees in Puerto Rico's manufacturing sector.

R-2092

-- Possessions corporations' tax savings in relation to their employment varied substantially by industry. In 1980, the tax savings per employee averaged $59,000 in the pharmaceutical industry and $4,000 in the low-technology industries. In all manufacturing industries, corporate tax savings per employee averaged $17,000.

-- As of year-end 1980, the book value of plant and equipment in Puerto Rico owned by possessions corporations in manufacturing was $1.5 billion.

-- By restricting to Puerto Rican source income the tax exemption on financial investments, the Tax Reform Act of 1976 induced possessions corporations to bring to Puerto Rico the large pool of funds that had been invested in the Eurodollar market. Total Puerto Rican financial assets held by exempt possessions corporations at year-end 1981 were $7.6 billion. At least through mid-1981, this large inflow of financial investment had a virtually imperceptible effect on the level of net capital flows into Puerto Rico, as there were offsetting flows of funds out of Puerto Rico, mainly through the banking system. Puerto Rico imposed new banking regulations effective February 1, 1982, which substantially tightened the rules governing the use of 936 funds by bankers, brokers, and Puerto Rican borrowers. The new regulations caused a decline in the interest rate on 936 deposits relative to Eurodollar deposits and appear to have resulted in a rise in the growth of Puerto Rican commercial loans.

An appendix to the Report summarizes the possessions corporation system of taxation as it relates to American Samoa and Guam. The appendix also describes the tax exemption for U.S. corporations operating in the Virgin Islands, which is delimited by section 934(b) of the Internal Revenue Code.

Copies of the Report are available for purchase from the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20401. When ordering, use Stock No. 048-000-00355-9.

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TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

FOR IMMEDIATE RELEASE March 16, 1983

RESULTS OF AUCTION OF 2-YEAR NOTES

The Department of the Treasury has accepted $7,758 million of $13,503 million of tenders received from the public for the 2-year notes, Series S-1985, auctioned today. The notes will be issued March 31, 1983, and mature March 31, 1985.

The interest rate on the notes will be 9-5/8%. The range of accepted competitive bids, and the corresponding prices at the 9-5/8% interest rate are as follows:

	Bids	Prices
Lowest yield	9.60% 1/	100.045
Highest yield	9.70%	99.867
Average yield	9.66%	99.938

Tenders at the high yield were allotted 71%.

TENDERS RECEIVED AND ACCEPTED (In Thousands)

Location	Received	Accepted
Boston	$ 162,285	$ 78,620
New York	10,528,375	5,904,265
Philadelphia	41,100	41,100
Cleveland	114,735	114,735
Richmond	141,210	139,340
Atlanta	139,795	137,925
Chicago	1,053,075	466,390
St. Louis	157,935	157,935
Minneapolis	100,020	99,730
Kansas City	174,965	172,820
Dallas	105,045	101,045
San Francisco	779,185	339,395
Treasury	5,155	5,155
Totals	$13,502,880	$7,758,455

The $ 7,758 million of accepted tenders includes $1,680 million of noncompetitive tenders and $ 6,078 million of competitive tenders from the public.

In addition to the $ 7,758 million of tenders accepted in the auction process, $710 million of tenders was awarded at the average price to Federal Reserve Banks as agents for foreign and international monetary authorities. An additional $600 million of tenders was also accepted at the average price from Government accounts and Federal Reserve Banks for their own account in exchange for maturing securities. (Such accounts may exchange additional amounts of maturing securities for the 4-year note to be auctioned on Tuesday, March 22, 1983.)

1/ Excepting 4 tenders totaling $1,510,000.

R-2093

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-204

FOR IMMEDIATE RELEASE March 17, 1983

RESULTS OF TREASURY'S 52-WEEK BILL AUCTION

Tenders for $ 7,751 million of 52-week bills to be issued March 24, 1983, and to mature March 22, 1984, were accepted today. The details are as follows:

RANGE OF ACCEPTED COMPETITIVE BIDS:

	Price	Discount Rate	Investment Rate (Equivalent Coupon-issue Yield)
High -	91.508a/	8.399%	9.12%
Low -	91.467	8.439%	9.17%
Average -	91.479	8.427%	9.16%

a/ Excepting 3 tenders totaling $1,100,000.

Tenders at the low price were allotted 78%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted
Boston	$ 179,510	$ 24,510
New York	14,406,290	6,894,800
Philadelphia	8,835	8,835
Cleveland	164,975	102,975
Richmond	89,045	60,970
Atlanta	67,190	66,090
Chicago	1,015,520	226,360
St. Louis	67,825	49,825
Minneapolis	37,830	27,830
Kansas City	41,120	41,120
Dallas	14,525	9,525
San Francisco	1,067,620	165,860
Treasury	71,835	71,835
TOTALS	$17,232,120	$7,750,535
Type		
Competitive	$14,769,740	$5,288,155
Noncompetitive	532,280	532,280
Subtotal, Public	$15,302,020	$5,820,435
Federal Reserve	1,500,000	1,500,000
Foreign Official Institutions	430,100	430,100
TOTALS	$17,232,120	$7,750,535

TREASURY NEWS
Department of the Treasury • Washington, D.C. • Telephone 566-2041

STATEMENT BY
DONALD T. REGAN
SECRETARY OF THE TREASURY
AT A PRESS CONFERENCE ON THE
DEMOCRATIC BUDGET PROPOSAL
MONDAY, MARCH 21, 1983
WASHINGTON, D.C.

The budget plan produced by the House Democratic Leadership and its Budget committee is an irresponsible blueprint for higher taxes and more spending which would, if adopted, abort the economic recovery.

This morning's release of the first quarter GNP deflator at 2.8 percent confirms the downward course of inflation. And that is reflected in the first quarter "flash" report of 4.0 percent GNP growth. If one listens closely, one can almost hear a roar.

It would be a tragedy for the Democrats to shut off this recovery just when hope for the unemployed is beginning.

Rather than working in a bipartisan way to reduce budget deficits, the House Democratic Leadership's plan calls for sharply higher taxes on working Americans to fund an enormous expansion of nondefense federal spending. It is a return to the type of budgets which gave us double-digit inflation, double-digit interest rates, and economic stagnation. We don't need more of that.

Such a proposal will surely reduce growth in the real Gross National Product. How much of a reduction in growth will occur is difficult to estimate; but the decline could be as much as 4 percentage points ($63 billion in 1972 dollars) by the end of 1985. If, as suggested by the revenue increases in the budget plan, the liberal Democrats were to repeal the third year of the President's tax cut and tax indexation, the resulting pressure on unit labor costs could reduce millions of jobs over the next several years.

If workers do not receive wage increases to cover the higher taxes proposed by these Democrats, then their standard of living will be reduced by such a proposal. If wage increases offset some of the higher taxes, then the higher labor costs to employers and work disincentives to employees could combine to worsen the employment prospects of millions of Americans. So, either way the American worker loses.

If the reduction in employment and the labor force is as great as could potentially occur, the resulting decline in our nation's real output would leave us with the economic stagnation characteristic of the last 5 years.

The massive tax increases called for in the budget could only be accomplished by the repeal of the third year of the tax cut and indexing.

Repeal of these tax cuts, just when the economy is struggling out of the recession, would be senseless and counterproductive, and would, as the Congressional Budget Office recently reported, prolong the recession and dampen any recovery.

The third year of the tax cut will help increase the savings rate, which has been falling lately, and bolster consumer spending which is still less than robust.

The liberal Democrats' tax increase would fall most heavily on the average working people of this country.

Seventy-two percent of the tax increase from a repeal of the third year and 78 percent of the tax increase from repeal of indexing would be paid by taxpayers earning less than $50,000.

The Democratic budget calls for a 24.3 percent tax increase for those earning less than $10,000, a 15 percent tax increase for those earning between $10,000 and $50,000, and only a 3.1 percent tax increase for those earning more than $200,000.

Low and middle-income taxpayers would bear the brunt of the tax increases. The repeal of the 3rd year and indexing would cost the typical median income family of four $1061 in higher taxes over the next three years and $3549 in higher taxes through 1988.

Higher taxes on the working people of this country will not solve our economic or budget problems. The House of Representatives should reject this preposterous budget proposal as unrealistic, unfair and unacceptable.

Change in Tax Liability Due to Repeal of the Third Phase of the Across-the-board Rate Reductions and Indexing

Four-person, One-earner, Median Income Families

(1983 $29,325)

(dollars)

	Calendar Years						:Cumulativ
	1983	1984	1985	1986	1987	1988	1983-88
Tax under current law	3,053	3,146	3,294	3,441	3,583	3,743	20,260
Tax under repeal of the third phase	3,238	3,519	3,685	3,850	4,010	4,188	22,490
Change from current law.	185	373	391	409	427	445	2,230
Percentage change	6|.1%	11.9	11.9	11.9	11.9	11.9	11.0
Tax under repeal of indexing	3,053	3,146	3,401	3,679	3,973	4,275	21,527
Change from current law.	--	--	107	238	390	532	1,267
Percentage change	0.0%	0.0	3.3	6.9	10.9	14.2	6.3
Tax under repeal of the third phase and indexing .	3,238	3,519	3,797	4,099	4,415	4,741	23,809
Change from current law.	185	373	503	658	832	998	3,549
Percentage change	6.1%	11.9	15.3	19.1	23.2	26.7	17.5

Office of the Secretary of the Treasury
Office of Tax Analysis

Note: Income increases are consistent with inflation assumptions in the January Budget economic scenario. For example, the annual assumed income for those earning $10,000 in 1980 is:

1983	1984	1985	1986	1987	1988
12,316	12,955	13,587	14,213	14,853	15,511

Tax calculations assume all income is wages and deductible expenses are equal to 23 percent of gross income.

Change in Tax Liability Due to Repeal of the Third Phase
of the Across-the-board Rate Reductions and Indexing

Four-person, One-earner Families

1980 Level of Income Income is assumed to grow at the inflation rate in every year	Calendar Years 1983	1984	1985	1986	1987	1988	Cumu 1
$10,000: ($12,316 in 1983)							
Tax under current law	611	673	702	731	758	792	4
Tax under repeal of the third phase and indexing ..	653	749	844	938	1,031	1,108	5
Change	42	76	142	207	273	316	1
Percentage change	6.9%	11.3	20.2	28.3	36.0	39.9	
$20,000: ($24,632 in 1983)							
Tax under current law	2,296	2,344	2,456	2,566	2,672	2,792	15
Tax under repeal of the third phase and indexing ..	2,426	2,633	2,841	3,072	3,308	3,552	17
Change	130	289	385	506	636	760	2
Percentage change	5.7%	12.3	15.7	19.7	23.8	27.2	
$30,000: ($36,948 in 1983)							
Tax under current law	4,501	4,647	4,864	5,082	5,295	5,531	29
Tax under repeal of the third phase and indexing ..	4,745	5,143	5,581	6,044	6,517	7,006	35
Change	244	496	717	962	1,222	1,475	5
Percentage change	5.4%	10.7	14.7	18.9	23.1	26.7	
$40,000: ($49,264 in 1983)							
Tax under current law	7,371	7,627	7,981	8,334	8,684	9,070	49
Tax under repeal of the third phase and indexing ..	7,783	8,512	9,231	9,945	10,674	11,493	57
Change	412	885	1,250	1,611	1,990	2,423	8
Percentage change	5.6%	11.6	15.7	19.3	22.9	26.7	
$50,000: ($61,580 in 1983)							
Tax under current law	10,741	11,093	11,606	12,120	12,634	13,194	71
Tax under repeal of the third phase and indexing ..	11,343	12,376	13,398	14,411	15,445	16,510	83
Change	602	1,283	1,792	2,291	2,811	3,316	12
Percentage change	5.6%	11.6	15.4	18.9	22.2	25.1	

Office of the Secretary of the Treasury
Office of Tax Analysis

Note: Income increases are consistent with inflation assumptions in the January Budget economic scenario. For example, the annual assumed income for those earning $10,000 in 1980 is:

1983	1984	1985	1986	1987	1988
12,316	12,955	13,587	14,213	14,853	15,511

Tax calculations assume all income is wages and deductible expenses are equal to 23 percent of gross income.

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-204

FOR IMMEDIATE RELEASE March 21, 1983

RESULTS OF TREASURY'S WEEKLY BILL AUCTIONS

Tenders for $6,200 million of 13-week bills and for $6,205 million of 26-week bills, both to be issued on March 24, 1983, were accepted today.

RANGE OF ACCEPTED COMPETITIVE BIDS:	13-week bills maturing June 23, 1983			:	26-week bills maturing September 22, 1983		
	Price	Discount Rate	Investment Rate 1/	:	Price	Discount Rate	Investment Rate 1/
High	97.879	8.391%	8.72%	:	95.692	8.521%	9.05%
Low	97.858	8.474%	8.80%	:	95.682	8.541%	9.08%
Average	97.868	8.434%	8.76%	:	95.685	8.535% 2/	9.07%

Tenders at the low price for the 13-week bills were allotted 31%.
Tenders at the low price for the 26-week bills were allotted 22%.

TENDERS RECEIVED AND ACCEPTED
(In Thousands)

Location	Received	Accepted	:	Received	Accepted
Boston	$ 116,555	$ 63,105	:	$ 148,700	$ 39,800
New York	10,070,695	4,569,745	:	14,449,115	5,327,000
Philadelphia	27,305	27,305	:	17,415	17,415
Cleveland	59,570	44,570	:	185,050	109,005
Richmond	54,565	44,565	:	198,065	34,785
Atlanta	49,415	49,415	:	67,415	44,615
Chicago	947,475	503,575	:	821,230	83,930
St. Louis	43,510	42,510	:	50,710	38,210
Minneapolis	45,705	45,015	:	21,225	15,225
Kansas City	63,185	58,685	:	39,360	39,360
Dallas	23,320	23,320	:	19,160	14,160
San Francisco	1,339,995	534,995	:	1,381,610	211,610
Treasury	193,325	193,325	:	229,855	229,855
TOTALS	$13,034,620	$6,200,130	:	$17,628,910	$6,204,970
Type					
Competitive	$10,859,305	$4,024,815	:	$14,978,875	$3,554,935
Noncompetitive	903,860	903,860	:	766,935	766,935
Subtotal, Public	$11,763,165	$4,928,675	:	$15,745,810	$4,321,870
Federal Reserve	1,266,355	1,266,355	:	1,225,000	1,225,000
Foreign Official Institutions	5,100	5,100	:	658,100	658,100
TOTALS	$13,034,620	$6,200,130	:	$17,628,910	$6,204,970

1/ Equivalent coupon-issue yield.
2/ The four-week average for calculating the maximum interest rate payable on money market certificates is 8.229%.

R-2096

TREASURY NEWS

Department of the Treasury • Washington, D.C. • Telephone 566-2041

TREAS.

HOLD FOR RELEASE
EXPECTED AT 9:30 A.M., EST
TUESDAY, MARCH 22, 1983

STATEMENT OF THE HONORABLE MARC E. LELAND
ASSISTANT SECRETARY OF THE TREASURY
FOR INTERNATIONAL AFFAIRS
BEFORE THE SUBCOMMITTEE ON INTERNATIONAL FINANCE
AND MONETARY POLICY
COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE

I am pleased to appear before this Subcommittee to support the Administration's proposed legislation to extend the Export-Import Bank Act until September 30, 1988. The Administration strongly supports a simple extension of the Eximbank Charter, with no amendments to the other provisions of the Act. Eximbank has done a good job of facilitating U.S. exports by countering foreign financing subsidies and overcoming deficiencies in private capital markets. We see no need to amend the existing Eximbank Charter. First, the existing Act has worked well. Secondly, the Charter contains the flexibility which enables the Administration and Eximbank to develop different approaches toward negotiating improved export credit arrangements. Finally, the Charter allows the Administration sufficient latitude to adapt policies to changing needs.

Reviewing and renewing the Eximbank Charter requires that we all step back from our experiences of the last five years and objectively determine the kind of Eximbank we want in the future. Much analysis of Eximbank has been distorted by our experiences in recent years, which have been characterized by heavily subsidized export credits. During this period, the primary objective of Eximbank has been to neutralize the effects of foreign export credit subsidies. The environment for trade finance, however, has been rapidly and dramatically changing in the last six months. Export credit subsidies are fading in importance, whereas ongoing developing country indebtedness has raised questions about the availability of adequate export finance.

None of us wants an Eximbank Charter armed with the weapons and strategy to fight the last war but totally inadequate to meet new challenges. For this reason, I would first like to outline the Administration's export credit policy. Secondly, I want to summarize our assessment of the export credit environment we will face during the next five years. In particular, my testimony will focus on our international efforts to eliminate export credit subsidies, the impact of lower commercial interest rates on officially supported finance, and the consequences of developing country indebtedness for trade finance. Thirdly, I would like to explain how the existing Eximbank Charter best enables the United States to position itself for the future. Revision of the Charter, in particular strengthening the Bank's competitiveness mandate, could severely handicap these efforts. Finally, at the request of the Committee, I would also like to discuss Administration views on Section 1912 of the Export-Import Bank Act Amendments of 1978, which deals with subsidized financing in the U.S. market.

Administration Export Credit Policy

The Economic Report of the President, transmitted to the Congress in February 1983, provides an excellent summary of the international economic foundations on which we have built U.S. export credit policy. I would like to highlight some of those conclusions today.

During the 1970's the world's market economies became more integrated with each other than ever before. Underlying the growth in world trade and investment was a progressive reduction of barriers to trade. In spite of its huge benefits, however, this liberalized trading system is now in serious danger. Within the United States, demands for protection against imports and for export subsidies have grown; a combination of structural changes, sectoral problems and short-run macroeconomic developments has led to a perception that we are becoming uncompetitive in world markets. It has further been argued that the position of U.S. business is steadily eroding in the international marketplace, primarily because of the support given to foreign businesses by their home governments.

The practices of foreign governments raise extremely difficult issues for U.S. trade policy. The United States has customarily sought to preserve and extend the benefits of free trade. To do this requires resisting protectionist pressures at home while continuing to work for the elimination of the more objectionable trade-distorting policies of all countries. Moreover, trade distorting policies such as export subsidies are equivalent to the multiple currency practices of the 1930's. They are precisely the same "beggar-thy-neighbor" competitive devaluation policies which contributed to the great international tensions of that time and which were only resolved by the Bretton Woods Agreement of 1945.

Export subsidies are a form of protectionism which the United States has pledged to avoid. Reintroduction of subsidies into the international trading system will only aggravate tensions arising from the global recession.

Trade-distorting measures, such as subsidizing exports, injure not only the competing countries, but the initiating country, even when they are a response to foreign trade-distorting practices. Obviously, export subsidies result in significant direct budgetary costs for the initiating country. In addition, the subsidy fails to improve the trade balance or generate economic growth even in the short run. Such subsidies benefit one industry at the expense of non-subsidized industries and other taxpayers. Moreover, at least part of an export subsidy is transferred abroad, as opposed to domestic subsidy programs.

If foreign governments subsidize exports on a large scale, world prices for U.S. products are depressed as a result. Large countersubsidies by the United States would depress prices still further. With floating exchange rates, an artificial increase in exports -- brought about by export subsidies -- increases demand for dollars, thus raising the exchange rate. This leads to a further loss of competitiveness in those sectors which are not promoted. Thus, departures from free trade are <u>not</u> called for, and if other countries do not play by the rules, we should target our responses and not try to launch large countersubsidy programs.

Intervention in international trade by the U.S. Government, even though costly to the U.S. economy in the short run, may be justified if it serves the strategic purpose of increasing the cost of interventionist policies by foreign governments. Thus, there is a potential role for carefully targeted measures -- explicitly temporary -- aimed at convincing other countries to reduce their trade distorting activities.

Consistent with the basic thrust of the President's Report, the Administration's export credit policy continues to be based on three precepts:

(1) We oppose export credit subsidies. Such subsidies transfer resources from domestic taxpayers to foreign importers, reduce the real gains from exporting, distort trade, and result in bloated government demands on credit markets.

(2) Export credit subsidies should be reduced and eventually eliminated through international agreement.

(3) In instances where such subsidies are applied, financing from the Export-Import Bank should be targeted to assist U.S. exporters to meet the competition where it is greatest.

Within this context, Eximbank has an important role to play in supporting U.S. exports against official foreign predatory financing, helping to overcome imperfections in capital markets, and maintaining pressure on other governments to negotiate reductions in their own export credit subsidies.

Export Credit Arrangement

We have made significant progress in our quest to eliminate export credit subsidies, an objective vigorously sought by both this and the previous Administrations. The U.S. Government has successfully negotiated improvements in the OECD Arrangement on Export Credits which have significantly raised the minimum interest rates offered by foreign export credit agencies over the past year and a half. For example, the minimum permissible rates for the most important credit recipients where most predatory financing has occurred were raised from 7.5 percent to 11.35 percent, an increase of 46 percent for those countries where most of the predatory financing has occurred. At the same time, commercial rates have declined as a result of our success in bringing down inflation. For a complete summary of these negotiations, I would like to refer the Subcommittee members to the September 16, 1982 report of the Department of the Treasury to the Congress entitled, "International Export Credit Negotiations (1981-1982)."

These two developments have dramatically changed the export credit picture in the past year. This recent convergence of officially supported interest rates and commercial interest rates has largely eliminated direct interest rate subsidies for most borrowers. Of the major trade financing currencies, only French franc interest rates are substantially higher than the current Arrangement rates, resulting in subsidies. Since a great deal of trade is financed in U.S. dollars (perhaps 40 percent or more), we have made a great stride in the right direction.

Given the present economic difficulties facing the Economic Community, it will take a great willpower and a firm commitment to free trade to hold this position. At upcoming negotiations we will concentrate our efforts on achieving a more flexible interest rate adjustment system that responds to market interest rate movements. This will not only be a more accurate system, it will remove the need for painstaking semiannual negotiations on interest rate levels. In addition, we have proposed measures to reduce government involvement in credits to the relatively rich countries. There was a preliminary negotiating session on March 1-2, and the Participants will meet again on April 25-27. If you wish, I could comment more on this during the question period.

Clearcut evidence of the success of our efforts is the recent Eximbank decision to revise the interest rates it charges on its loans. The Board reduced interest rates to the lowest levels permitted under the International Arrangement, without jeopardizing its financial position whatsoever. Thus, a major goal of this Administration and previous Administrations has been achieved.

We were successful in obtaining agreement from all Participants to a prohibition of mixed credits with a concessionality level of less than 20 percent. This prohibition took effect last October 15, as a specific part of the pledge not to derogate with respect to interest rate or repayment term. Previously, this category of mixed credits had been permitted, with prior notification to other Participants. This made it relatively easy for Participants to "buy" exports by adding a small amount of aid money to their financing.

The U.S. Government is pressing for even tighter discipline over mixed credits, and has proposed (1) a ban of all mixed credits that are not foreign aid, by raising the minimum permitted level of concessionality from 20 up to 25 percent; (2) prior notification for mixed credits with grant elements greater than 25 percent; and (3) a ban of mixed credits offered as lines of credit. By raising the minimum grant level, it becomes more costly for countries to offer mixed credits for export promotion, in terms of both budgetary cost and diversion of scarce aid resources.

Developing Country Indebtedness

Since about the middle of last year, the international monetary system has been confronted with serious financial problems which have arisen as a result of the size of the debt of several key countries, the turn in the world economic environment, and inadequacy of adjustment policies. In response, lenders began to retrench sharply, and the borrowing countries have since been finding it increasingly difficult to raise money to pay for essential imports. Last year, net new bank lending to non-OPEC LDCs dropped by roughly half, to about $20-25 billion for the year as a whole, and came to a virtual standstill for a time at midyear.

The only fast way for these countries to reduce their deficits significantly in the face of an abrupt cutback in financing is to cut imports drastically, either by sharply depressing their economies to reduce demand or by restricting imports directly. Both of these are damaging to the borrowing countries and painful to industrial economies like the United States -- because almost all of the reduction in LDC imports must come at the direct expense of exports from industrial countries. But as the situation has developed in recent months, there has been a danger that lenders might move so far in the direction of caution that they compound the adjustment and liquidity problems already faced by major borrowers, and even push other countries which are now in reasonably decent shape into financial problems as well.

In order to appreciate fully the potential impact on the U.S. economy of rapid cutbacks in LDC imports, it is useful to look at how important international trade has become to us. Trade was the fastest growing part of the world economy in the last decade -- but the volume of U.S. exports grew even faster in the last part of the 1970's, more than twice as fast as the volume of total world exports. By 1980, nearly 20 percent of total U.S. production of goods was being exported, up from 9 percent in 1970, although the proportion has fallen slightly since then. High-technology manufactured goods are a leading edge of the American economy, and, not surprisingly, net exports of these goods have grown in importance. The surplus in trade in these products rose $7.6 billion in 1970 to $30 billion in 1980. Our trading relations with non-OPEC LDCs have expanded even more rapidly than our overall trade. Our exports to the LDCs, which accounted for about 25 percent of total U.S. exports in 1970, rose to about 29 percent in 1980. In manufactured goods, which make up two-thirds of our exports, the share going to LDCs rose even more strongly -- from 29 percent to 39 percent. What these figures indicate is that the export sector of our economy is vulnerable to any sharp cutback in imports by non-OPEC developing countries.

An essential element in resolving debt problems is continued commercial bank lending to countries that are pursuing sound adjustment programs. In the last months of 1982 some banks, both in the United States and abroad, sought to limit or reduce outstanding loans to troubled borrowers. But an orderly resolution of the present situation requires not only the willingness by banks to roll over or restructure existing debts, but also to increase their net lending to developing countries, including the most troubled borrowers, to support effective, nondisruptive adjustment.

The Administration is launching a major effort to respond to the increased indebtedness and balance of payments problems in many developing countries. The primary focus of this effort has been the International Monetary Fund, for which we are seeking a substantial increase in resources. Commercial lenders are increasing their lending, but with these increases, there is an important role for government guarantees during this transition period. Consequently, the support of Eximbank will be an important element in the total U.S. Government effort to provide a "credit bridge" across which trade can flow until recovery begins.

Eximbank in the New Economic and Financial Environment

Much lower interest rates in all SDR currencies, coupled with much higher interest rate minima under the Arrangement than a year ago, present an opportunity for Eximbank to make increasing use of guarantees and insurance authority in the provision of competitive financing offers. Moreover, current trends in U.S. market rates and the expected financial status of many developing country borrowers may well enhance the shift of demand from credits to guarantees, since commercial lenders may require this additional inducement to increase trade credit to some countries.

Thus, the critical issues for trade finance are shifting in this new environment. Export credit subsidies will fade and perhaps disappear as key elements in export credit competition. Instead, the availability of export finance will take center stage in a world in which commercial export credits may become more difficult to obtain.

The existing Eximbank Charter will enable the United States to respond effectively to this rapidly evolving economic and financial environment. The primary legislative objective of the Bank is to aid in financing and to facilitate U.S. exports. The Bank will continue to support U.S. exports. On account of the success of Arrangement negotiations and falling commercial rates, an increasing share of Eximbank support over the next five years will take the form of guarantees and insurance. Most importantly, the Charter ensures that Eximbank's excellent guarantee and insurance programs are poised to do their part in providing a "credit bridge" to a number of developing countries. No amendment to the Charter is necessary to implement our basic policy to place increased emphasis on guarantees and insurance.

The current Charter enumerates a number of objectives, goals, and policies for Eximbank. In terms of Eximbank's actual operations, the Administration believes that the following have been and should continue to be the primary operational policies of the Bank:

-- to offer rates and terms competitive with foreign rates and terms;

-- to seek to minimize competition in government-supported export credits;

-- to supplement and encourage, and not compete with, private capital;

-- to offer rates taking into consideration the average cost of money to the Bank as well as the need to be competitive;

-- to offer loans for specific purposes with a reasonable assurance of repayment; and

-- to deny credit applications for nonfinancial noncommercial considerations only if the President determines that such action would be in the national interest.

Eximbank has been and is competitive. Eximbank offers interest rates for direct credits fully competitive with foreign officially supported interest rates and even offers foreign currency guarantees to neutralize the advantages of low interest rate countries such as Japan and Germany. In addition, Eximbank's guarantee and insurance programs are ready to respond effectively in the new competitive arena for trade finance, namely the increased importance of credit availability in keeping exports flowing.

The Bank will have ample budget authority to meet its objectives. For FY 1984, the Administration is requesting $3.8 billion in direct credits and $10.0 billion in guarantees and insurance. These requests reflect the Administration's view that credit availability rather than subsidized financing will emerge as the key trade credit issue. If subsidized foreign export credits again become a major problem, the Administration has pledged to seek up to an additional $2.7 billion in direct credit authority. In short, we are poised to use Eximbank as leverage against foreign export credit subsidies; no additional legislative mandate is required.

The genesis of recent proposals to strengthen further the competitiveness mandate was the Eximbank decision in July, 1981, to raise interest rates above Arrangement rates and to charge an application fee in order to offset its deteriorating financial position. The new rates were 1.5-2.0 percentage points above Arrangement rates, but still as much as 5.0 percentage points below Eximbank's own cost of money, and as much as 10 percentage points below commercial rates. A few cases were lost because of financing. But the new rates helped protect Eximbank's accounts from a hemorrhage of its capital and reserves. The Bank did suffer losses, but those losses were contained within reasonable limits.

The Administration believes that efforts to strengthen the competitiveness mandate are unnecessary. In formulating Eximbank policy, we recognize that it is very important for Eximbank to be competitive. Eximbank already provides financing on terms and conditions which enable U.S. suppliers to compete for export sales. Revising the present mandate could imply that the Bank must exactly match foreign subsidies (including foreign aid) in all cases. This would be potentially costly and undermine the

Administration's flexibility. First, it would make it more difficult for the Administration to limit the cost of export subsidies during periods of inflation, thereby sheltering exports relative to other sectors of the economy. Secondly, it would permanently lock Eximbank into providing subsidized financing. U.S. Government export credit subsidies are costly and are only justified if they are carefully targeted, explicitly temporary, and aimed at the strategic purpose of convincing other countries to reduce trade distortions. Finally, it would undermine our flexibility to develop different approaches toward negotiating improvements in export credit arrangements.

The other legislated policies of Eximbank allow plenty of latitude for the Bank and the Administration to deal with the emerging economic and financial environment. We can not afford to lose sight of the Bank's cost of funds in setting interest rates, particularly in the context of our efforts to control the Federal deficit. Eximbank's response to the credit availability problem is fully in line with the requirement to supplement, not compete with, private capital markets. Balancing this, the legislative requirement that there is a "reasonable assurance of repayment" for each transaction ensures that the Bank does not assume overwhelming commercial and political risks. Our ongoing efforts to improve the Export Credit Arrangement and the increased Eximbank use of guarantees and insurance are consistent with the mandate to minimize export credit subsidies. In our view, none of these objectives should be de-emphasized in the course of charter renewal. They all represent statements of important policy goals which, taken as a group, allow us to respond to the financial environment we expect.

Section 1912, Export-Import Bank Act Amendments of 1978

One trade finance issue which has become particularly acute in the past year is the question of how the United States should respond to offers of subsidized foreign financing for imports into our market. This issue received substantial attention in connection with the sale of Canadian subway cars to New York's Metropolitan Transportation Authority.

The Administration pursued a number of remedies in the MTA case. A significant countervailing duty finding was made by the Commerce Department and the Treasury conducted an investigation under Section 1912 of the Export-Import Bank Act Amendments of 1978.

The latter section empowers the Secretary of the Treasury, under certain conditions, to authorize matching financing from Eximbank for U.S. producers if "noncompetitive" financing by a foreign government is "likely to be a determining factor" in a sale in the United States. As a major participant in the drafting of this legislation, the Chairman knows that the law defines "noncompetitive" as any financing which exceeds limits prescribed by international understandings on export credits. Thus, the statute wisely requires policy judgments, first as to whether Eximbank financing could be offered, and then as to whether it should be offered.

Context and Goals. Section 1912 was designed, of course, (a) to help U.S. industry cope with subsidized competition, and (b) to backstop U.S. efforts to negotiate an end to subsidized trade finance. It is intended to be prospective rather than, as is generally true of the countervailing duty law, retrospective. Unlike the countervailing duty law, Section 1912 does not deal with injurious import competition since it requires no injury test.

But Section 1912 adds a most useful new weapon to the U.S. arsenal at a time when we are trying to persuade other major exporting nations not to subsidize trade finance. By focusing on derogations from the Arrangement's discipline, the statute reinforces U.S. efforts to eliminate export credit subsidies. It also conserves Eximbank resources for use when foreign subsidies are most objectionable. It applies directly to subsidies that are prima facie violations of the Subsidies Code. Finally, Section 1912 complements our countervailing duty law, which targets a broader range of practices not necessarily violative of international agreements but possibly harmful to U.S. industry.

Should Section 1912 be Amended? This review of Section 1912's place in our trade strategy suggests that it serves our purposes well just as it is. The high visibility given Section 1912 proceedings by the requirements for (a) a direct approach to the subsidizing government, and (b) the personal involvement of the Secretary of the Treasury is in itself a significant contribution to the attainment of U.S. policy objectives. We believe that the use of matching Eximbank financing can, in the right circumstances, be a similarly useful option under the statute as now drafted.

We see a danger in amending Section 1912 to make the provision of Eximbank financing to U.S. entities more automatic. This is that the statute, instead of being a tool for enforcement of U.S. trade policy, could become an entitlement program for any U.S. purchaser which can point to an offer of subsidized foreign competition. Indeed, some of the amendments which have been suggested could have the effect of encouraging U.S. purchasers to seek foreign competition in order to trigger an offer of Eximbank funding. The paradoxical result could be to institutionalize, rather than discourage, subsidized credit competition.

For these reasons, we strongly believe that the statute must continue to permit discretion in its application if it is to fulfill its purpose of helping to keep U.S. industry competitive while discouraging wasteful credit subsidies.

Conclusion

In light of the rapidly evolving economic and financial environment, the Administration and Eximbank require the latitude to respond to changing needs. The current provisions of the Export-Import Bank Act provide the needed flexibility.

The Charter has worked well, even during a difficult period when heavily subsidized export credits were the central trade finance issue. With the virtual elimination of export credit subsidies, we see no need to strengthen further the Bank's competitiveness mandate, particularly since competitiveness has been a primary goal of the Bank's operations over the last five years. Finally, we believe that Section 1912 must continue to permit discretion in its application.

The Administration urges Congress to extend the Act for five years, but not to amend the existing provisions. In our view, it makes no sense "to fix somethin' that ain't broke."

TREASURY NEWS

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FOR IMMEDIATE RELEASE
Thursday, March 22, 1983

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202/566-2041

NOTE TO CORRESPONDENTS

William S. McKee, Tax Legislative Counsel for the U.S. Department of Treasury, has been named Acting Deputy Assistant Secretary (Tax Policy). He will serve in this position pending the selection of a replacement for the former Deputy, David G. Glickman, who recently returned to the private sector. Mr. McKee also has announced his plans to return to the private sector in the near future.

Assuming Mr. McKee's position, also on an acting basis, is Robert Woodward who is currently Associate Tax Legislative Counsel. Both Mr. McKee and Mr. Woodward are attorneys.

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FOR IMMEDIATE RELEASE
Tuesday, March 22, 1983

CONTACT: Robert D. Levine
202/566-2041

SECRETARY REGAN APPOINTS CAROLE DINEEN FISCAL ASSISTANT SECRETARY

Secretary Donald T. Regan today appointed Carole Jones Dineen, 41, of New York City to be Fiscal Assistant Secretary at the Department of the Treasury.

As Fiscal Assistant Secretary, Ms. Dineen will oversee the Treasury Department's management of the U.S. Government's financial operations, cash management for the U.S. Government, raising money to finance government debt, directing the performance of the fiscal agency functions of the Federal Reserve Banks and handling the investments of the multi-billion dollar trust and other accounts of the U.S. Government.

Secretary Regan said: "Carole's strong line management and banking skills, her experience with computerized financial operations, and her accomplishments in two important service industries qualify her superbly for the demanding and complex responsibilities she will be undertaking at Treasury.

"Carole will play a major role in modernizing the government's financial operations. And, under the President's Reform '88 program, Carole Dineen is being designated as the head of all cash management activities for the Federal Government. I am confident she will bring the same modern management techniques to the Federal Government that she has introduced in private industry. We are delighted to have her."

Ms. Dineen has been a Vice President at the Bankers Trust Company in New York in three different capacities during the past five years. She was responsible for Money Transfer Customer Service, Deposit Accounting and Commercial Account Operations. Before that she was with Trans World Airlines for ten years, last as the manager of operations at JFK Airport in New York. Ms. Dineen graduated from the honors program of Brown University in Providence, Rhode Island.

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