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Office Memorandum

TO : Secretary Anderson

DATE: November 8, 1960

FROM : Frank A. Southard, Jr. FAS

SUBJECT : Use of Fund Resources by the United States

I have thought further about the ways in which the United States might use the Fund's resources and I am summarizing below some possibilities.

1. If the only purpose is to ease somewhat a current dollar drain, the United States could simply draw moderate amounts of needed currencies such as deutsche marks. We could also draw certain currencies as an offset against dollar drawings. For example, if Venezuela insists on drawing $25 million, the United States could draw deutsche marks to that same amount. This would cost us 1/2 of 1 per cent but we might recoup this by selling the deutsche marks at the current dollar rate, since the deutsche mark is at a premium. However, I am hopeful that ways will be found to make it easy for countries to draw currencies other than dollars.

2. The important question is how the United States might make large Fund drawings with the effect of preventing gold outflows. The problem is not easy because, if a country like Germany were determined to convert current dollar holdings into gold, even a large U.S. drawing of deutsche marks would not prevent this, although it would prevent a corresponding increase in German dollar holdings. I see two possibilities as follows, and I shall use Germany and the deutsche mark as the example, although the same analysis could apply to any other suitable country and currency such as the United Kingdom, Italy or Japan.

(a) The United States could arrange with Germany that, when Germany had "excess dollars" which it was thinking of converting into gold, the United States would draw deutsche marks from the Fund and exchange them for the dollars. The result would be that the United States would owe the Fund and that Germany would have a gold-secured "credit" in the Fund. This process could be repeated any number of times. Moreover, from time to time Germany could convert some of its credit position with the Fund into gold by asking the Fund to replenish IMF holdings of deutsche marks by a sale of gold to Germany.

(b) In effect the United Kingdom has been carrying out this process directly with the Fund in recent months, by voluntarily handing excess dollars to the Fund instead of demanding gold from the United States. This was possible because the United Kingdom was in debt to the Fund. The United Kingdom is out of debt to the Fund but there still remains about $89 million which the United Kingdom could voluntarily pay to the Fund so as to bring the Fund's holdings of sterling down to 75 per cent of quota -- for technical reasons the United Kingdom is not yet legally obligated to do this although most countries outside of the sterling area have done so. I believe U.K. officials are giving some thought to carrying out this voluntary operation which would, to that extent, cut down U.K. conversions of dollars into gold. You could express

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some appreciation to Lord Cromer for U.K. willingness to make the recent voluntary repurchases, and tell him that you would welcome this last voluntary step, or I could say this to him and associate you with it. What do you think?

(c) By another technique there could be three simultaneous transactions: The United States would draw deutsche marks; the Fund would buy deutsche marks with gold; and the United States would exchange the deutsche marks for the gold. The result would be that the United States would receive gold from the Fund (which would offset gold losses to various central banks being incurred at the same time), and the United States would owe the IMF for the total value of the operation. The German position would be unchanged. There is nothing technically wrong with this scheme, but it may be difficult to "sell" to other Directors, and in any case it could not be worked until Germany is under Article VIII. The scheme outlined in (a) above would be much easier to work out.

3. The advantage of the above arrangements would be that they would either prevent a drain of gold or would offset a gold drain by an acquisition of gold from the Fund, depending on whether (a) or (c) was used. Alternatively, if the United States at a time of heavy gold loss were simply to make large drawings of marks or sterling or yen from the Fund, it would by no means be certain that the U.S. gold position would be protected. True, central banks would not be accruing dollars as rapidly, because the United States would be covering its own needs in those currencies by Fund drawings instead of buying the currencies against dollars in the market. But in the meantime the countries might continue converting their existing dollar balances into gold. Moreover, the Fund would probably have to replenish its holdings of those currencies by gold sales to them, so that they might get gold in two directions, from the United States and from the Fund.

4. I am writing this memorandum primarily to raise for consideration this question: Should we find some way of exploring with key countries the possibilities outlined in paragraph 2? If we wait until the last minute all we could do would be to fall back on drawings as in paragraph 3.

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