1965 ANNUAL REPORT

INTERNATIONAL MONETARY FUND

ANNUAL REPORT
1965

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INTERNATIONAL MONETARY FUND

ANNUAL REPORT

OF THE

EXECUTIVE DIRECTORS FOR THE

FISCAL YEAR ENDED APRIL 30, 1965

WASHINGTON, D. C.

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CONTENTS

Chap.		*Page*
	Letter of Transmittal	xiii

PART I. THE WORLD ECONOMY AND THE FUND

1.	GENERAL SURVEY	3
	International Payments	4
	Primary Producing Countries	6
	Countries' Reserves and International Liquidity	8
2.	THE INTERNATIONAL MONETARY SYSTEM AND INTERNATIONAL LIQUIDITY	9
	Characteristics of the System	9
	Appraisal of the System	11
	Role of Capital Movements	12
	Scope for Adjustment of Price Levels	13
	Role of Reserve Currencies	13
	Types of International Liquidity	14
	Potential Need to Supplement Growth of Reserves	15
	Deliberate Reserve Creation	15
	Criteria of General Reserve Needs	16
	Types of Reserve Creation	16
	Transferability of Reserves: Direct and Indirect	16
	Distribution of Initial Reserve Increases	17
	Institutional Aspects	18
	Reserve Creation Through the Fund	18
	Conclusion	19
3.	SOME PROBLEMS OF DEVELOPING COUNTRIES	20
	Introduction	20
	Fiscal Systems	21
	The Problems	21
	Steps to Strengthen Public Finances	22
	Budgetary Planning and Control	22
	Tax Reform	22
	Tax Administration	23
	Pricing Policies of Public Enterprises	23
	Debt Burdens and Debt Renegotiation	23
	The Problem	23
	Debt Repayment Schedules	24
	Renegotiation Possibilities	26
	Present Practices in Debt Renegotiation	27
	Conditions for Success	28
	The Role of the Fund	29
	Conclusion	30

Chap.	Page
4. The Fund in 1964/65	31
Membership	31
Article VIII	31
Executive Directors	31
Increase in Fund Resources	31
Proposals for Quota Increases	32
Size of Quota Increases	32
Gold Payments and Their Alleviation	33
Fund Transactions	34
Purchases and Stand-By Arrangements	34
Technical Assistance	36
The IMF Institute	37

PART II. REVIEW OF THE YEAR

5. Developments in the Industrial Countries	41
Production, Wages, and Prices	41
Incomes Policies	44
Financial and Other Policy Developments Before November 1964	45
Discount Rates	45
Monetary and Debt Management Policies	45
Fiscal Policy	47
Subsequent Events	47
The Problems	47
Changes in Policy	48
Foreign Exchange Markets	50
Development of Securities Markets	50
6. World Trade, Payments, and Reserves	53
World Trade	53
Changes in Trade, 1963-64	53
Trade in Manufactures	54
Export Growth and Market Growth	57
Development of World Trade During 1964	58
Private Capital Movements	60
Balance of Payments Developments	63
Current Account and "Basic" Balances	63
Over-All Surpluses and Deficits	66
Reserve Developments	68
7. Developments in Countries Exporting Primary Products	70
Prices	70
Trade	71
Balance of Payments	73
More Industrialized Countries	73
Less Industrialized Countries	75
Domestic Developments	78
8. Balances of Payments of Selected Countries	79
United States	79

Chap. *Page*

Canada 82
United Kingdom 83
Federal Republic of Germany 85
France 85
Italy 88
Japan 89
Australia 91
Brazil 91
Ghana 92
India 93
Mexico 95

9. GOLD 96
Gold Production 96
Gold Holdings 97
Gold Markets and Prices 99
New York 99
London 99
Other Developments 101
Gold Transactions Service 102
Changes in National Policies Affecting Gold 102
Gold Subsidy Programs 102

SUPPLEMENTARY NOTE

ACTIVITIES OF THE FUND 107
Par Values 107
Article VIII Countries 107
Quotas 107
Fund Transactions 108
Stand-By Arrangements 109
Repurchases 111
Purchases and Repurchases Classified by Currency 112
Monetary Reserves and Repurchase Obligations 113
Summary of Transactions, 1948-65 114
Fund Charges 116
Consultations with Members 116
Relations with Other International Organizations 117
Staff 118
Publications 118
Administrative Finance 119

APPENDICES

No.

I. Executive Board Decisions and Report to Board of Governors 123
A. Calculation of Repurchase Obligations: Prompt Reporting of Monetary Reserves Data 123

Page

B. Procedure for Drawings in the Gold Tranche 123
C. Increases in Quotas of Members—Fourth Quinquennial Review 124
II. Executive Directors and Voting Power 133
III. Changes in Membership of Executive Board 136
IV. Administrative Budget 140
V. Comparative Statement of Income and Expenditure 142
VI. Financial Statements 143
International Monetary Fund 145
Staff Retirement Fund 150
Index 155

LIST OF TABLES AND CHARTS

Table *Page*

1. Thirty-Seven Countries: Annual Service Charges on Medium-Term and Long-Term External Debt, End of Year, 1956-64 24
2. Thirty-Seven Countries: Medium-Term and Long-Term External Public Debt, End of Year, 1956-64 25
3. Thirty-Seven Countries: Annual Service Charges on Medium-Term and Long-Term External Public Debt as Percentages of Outstanding Debts, End of Year, 1956-64 25
4. Short-Term Claims on Selected Countries Reported by U.S. Banks and Nonfinancial Concerns, End of Year, 1960-64 26
5. Proposed Increases in Quotas, 1965: Special Increases 32
6. Gross National Product at Constant Prices: Percentage Increases from Quarter to Quarter, 1962–First Quarter 1965 42
7. Industrial Production: Percentage Changes from Quarter to Quarter, 1962–First Quarter 1965 43
8. Issues of Securities on Markets in Countries Other than That of Borrower, 1963–First Quarter 1965 51
9. Foreign Issues of Securities in Currency of Market Where Issued, 1963–First Quarter 1965 51
10. Amounts Raised by Issues of Securities on Markets in Countries Other than That of Borrower, 1963–First Quarter 1965 51
11. Sales of New Issues by Foreign Borrowers in the United States, 1963–First Quarter 1965 51
12. Export Unit Values, 1961-64 53
13. Direction of World Trade, 1963 and 1964 53
14. Growth in Value of Trade Between Major Areas, 1961-64 54
15. Trade Between Manufacturing Countries, 1963 and 1964 55
16. United Kingdom: Value and Growth of Trade in Three Major Categories, 1964 55
17. Growth of Manufacturing Countries' Trade in Machinery and Transport Equipment and Other Manufactures, by Areas 56
18. Value of Manufacturing Countries' Trade in Machinery and Transport Equipment, Other Manufactures, and All Other Goods, January-September 1964. 57

Table		Page
19.	EEC Countries: Imports of Manufactures from Each Other and from the United States, January-September, 1964	57
20.	Manufacturing Countries: Changes in the Relation Between Each Country's Export Unit Value and the Average Unit Value of Other Countries' Exports, 1963-64	57
21.	Manufacturing Countries: Actual Growth in Each Country's Exports Related to Average Growth in Its Export Markets, 1962-64	58
22.	Net Outflows of Private U.S. Capital, 1963 and 1964	61
23.	EEC Countries: Balance of Payments Summaries, 1963 and 1964	62
24.	Other Manufacturing Countries in Continental Europe: Balance of Payments Summaries, 1963 and 1964	63
25.	Over-All Balances of International Payments, 1963 and 1964	67
26.	Countries' Official Reserves, Including Reserve Positions in the IMF, End of Calendar Years, 1961-64	68
27.	Countries Exporting Primary Products: Indices of Commodity Prices, 1962–First Quarter 1965	70
28.	Primary Producing Countries: Trade in 1963 and 1964	74
29.	Primary Producing Countries: Balance of Payments Summaries, 1963 and 1964	76
30.	United States: Balance of Payments Summary, 1963–First Quarter 1965	80
31.	Canada: Balance of Payments Summary, 1963–First Quarter 1965	82
32.	United Kingdom: Balance of Payments Summary, 1963–First Quarter 1965	83
33.	Federal Republic of Germany: Balance of Payments Summary, 1963–First Quarter 1965	86
34.	France: Balance of Payments Summary, 1963 and 1964	87
35.	Italy: Balance of Payments Summary, 1963 and 1964	88
36.	Japan: Balance of Payments Summary, 1963–First Quarter 1965	90
37.	Australia: Balance of Payments Summary, 1961-64	91
38.	Brazil: Balance of Payments Summary, 1961-64	92
39.	Ghana: Balance of Payments Summary, 1961-64	93
40.	India: Balance of Payments Summary, 1961-64	94
41.	Mexico: Balance of Payments Summary, 1961-64	94
42.	Gold: Value of World Production, 1940, 1945, and 1960-64	96
43.	World Gold Reserves: Sources of Changes, 1962-64	99
44.	U.S. Gold Transactions, 1963 and 1964	99
45.	Gold: Prices in Various World Markets, End of April 1964 and 1965	101
46.	Initial Par Values Established, Fiscal Year Ended April 30, 1965	107
47.	Countries That Have Accepted Article VIII	107
48.	Increases in Quotas, Fiscal Year Ended April 30, 1965	108
49.	Purchases of Currencies from the Fund, Fiscal Year Ended April 30, 1965	108
50.	Position of Participants in General Arrangements to Borrow	108
51.	Currencies Purchased by the Fund with Gold, December 1964 and May 1965	108
52.	Fund Stand-By Arrangements with Members, Fiscal Year Ended April 30, 1965	109
53.	Repurchases of Currencies from the Fund, Fiscal Year Ended April 30, 1965	112
54.	Drawings and Repurchases by Currency, Fiscal Year Ended April 30, 1965	113
55.	Repurchase Obligations Under Article V, Section 7(*b*), of the Fund Agreement, at April 30, 1948-64	114
56.	Summary of Fund Transactions, Fiscal Years Ended April 30, 1948-65	116

Chart *Page*

1. Thirty-Seven Countries: External Public Debt Service as Percentage of Exports, 1956-64 26
2. Seven Latin American Countries: External Public Debt Service as Percentage of Exports, 1955, 1960, and 1964 26
3. Selected Areas and Countries: Industrial Production, Seasonally Adjusted, 1961–April 1965 41
4. Selected Countries of the European Economic Community: Industrial Production, Seasonally Adjusted, 1961–April 1965 42
5. Selected Areas and Countries: Wage Rates, 1961–April 1965 43
6. Selected Countries: Wage Costs per Unit of Output in Manufacturing, 1961-64 43
7. Selected Areas and Countries: Import Prices, 1961–First Quarter 1965 44
8. Selected Areas and Countries: Wholesale Prices, 1961–April 1965 44
9. Selected Areas and Countries: Cost of Living, 1961–April 1965 44
10. Selected Areas and Countries: Export Prices, 1961–April 1965 44
11. Selected Countries: Central Bank Discount Rates, 1961–April 1965 45
12. Selected Countries: Term Structure of Interest Rates 46
13. Selected Countries: Exchange Rates, 1961–April 1965 47
14. Covered Short-Term Interest Rates, 1961–April 1965 48
15. United Kingdom: Term Interest Differentials, 1963–April 1965 48
16. Selected Countries: Long-Term Government Bond Yields, 1961–April 1965 49
17. U.K. External Sterling Liabilities, 1961–March 1965 50
18. U.S. International Liquid Liabilities, 1961–March 1965 50
19. Volume of World Exports and Seasonally Adjusted Volume of Exports and Imports of Four Major Areas, Quarterly, 1961-64 58
20. EEC Countries, United Kingdom, and Other EFTA Countries: Volume of Trade, Seasonally Adjusted, Quarterly, 1961-64 59
21. Manufacturing Countries: Seasonally Adjusted Trade Balances, 1961–First Quarter 1965 60
22. Selected Areas and Countries: Balances of Payments, 1957-64 64
23. All Countries in Balance of Payments Deficit: Aggregate Deficits, 1958–First Quarter 1965 68
24. Primary Producing Countries: Prices of Commodities Exported (Excluding Petroleum), 1962–First Quarter 1965 71
25. Selected Primary Products: Changes in Average Prices in 1963 and 1964 .. 72
26. Primary Producing Countries: Balances of Payments, 1957-64 77
27. Primary Producing Countries: Basic and Over-All Balances of Payments, 1957-64 78
28. Gold: Estimated Supply and Absorption, 1951-64 98
29. Gold: Price in London Market, Monthly Averages, March 1954–April 1965 100
30. Outstanding Balances of Drawings from the Fund, and Unused Stand-By Arrangements, on April 30, 1948-65 115

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LETTER OF TRANSMITTAL
TO THE BOARD OF GOVERNORS

July 2, 1965

My dear Mr. Chairman:

In accordance with Section 10 of the By-Laws of the International Monetary Fund, I have the honor to present to the Board of Governors the Annual Report of the Executive Directors for the fiscal year ended April 30, 1965.

Yours sincerely,

/s/

PIERRE-PAUL SCHWEITZER

Chairman of the Executive Board

Chairman of the Board of Governors

International Monetary Fund

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Part I

THE WORLD ECONOMY AND THE FUND

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Chapter 1

General Survey

IN many respects the past year was a highly satisfactory one for the world economy. World industrial production and, in particular, international trade—including the exports of the primary producing countries—were substantially higher than in the preceding year. However, within 1964 there was a slowing down of economic activity in several major countries, and the rate of increase in world trade was somewhat lower than during the preceding year, although still substantial. In the last quarter of the year, while there were signs of a moderate upturn in industrial activity, an exceptionally large imbalance in world payments, concentrated in the two main reserve centers, put more strain on the international monetary system than had been experienced for some time. For all these reasons, economic prospects at the end of the year appeared much more uncertain.

During 1964 and the early months of 1965, economic activity continued to expand in the United States and Canada under conditions of substantial price stability, while some further progress was made toward reducing the relatively high rate of unemployment. In Europe, high levels of employment and strong pressures on wages and prices continued in most countries, although their experience was by no means uniform. In Germany, an acceleration in economic activity had been stimulated in 1963 by acute demand pressures in neighboring countries, mainly Italy and France. Throughout 1964, production continued to rise strongly, as an increase in domestic demand made up for a relaxation of demand pressures emanating from these other countries; prices rose only moderately. In Italy, pressures of demand were threatening both internal and external stability at the beginning of 1964. However, the economic policies which had been introduced progressively after May 1963 brought about a dramatic change from a large deficit to a large surplus in the balance of payments, and some slowing in the rise in prices and wages—but also a decline in industrial production until late in the year. In France, where policies to stabilize the economy were pursued throughout 1964, the rise in industrial production came virtually to a halt, and some progress was made in reducing the upward movement of prices. In a few other countries in continental Europe, where the containment of inflationary pressures had also become the primary objective of economic policy, there was a deceleration of the rise of output in the course of the year.

In the United Kingdom, the rise in production during 1964 was markedly less than in 1963, when it had been unusually large and had been accompanied by a gradual deterioration in the current account of the balance of payments. The budget introduced in April 1964 was aimed at limiting the rise in demand so as to correspond to a rise in real output of some 4 per cent per annum. However, despite this adjustment in policy, a large deficit in the balance of payments persisted through the year; the measures taken to deal with this are described below. At the beginning of 1964, Japan, too, was facing a balance of payments deficit, and this was a main factor limiting the rise in production. Here, however, effective measures to adjust the balance of payments, necessitated by the very rapid expansion in domestic demand that had taken place in 1963, were introduced at an early stage. During 1964, the rise of output slowed down moderately, and the balance of payments recovered; by the end of the year, the Japanese Government was relaxing its policies of economic restraint.

The net result of these developments was that late in 1964 the forces of expansion operating in the industrial countries as a group were less vigorous than at the beginning of the year. Some slowing down in economic growth was perhaps to be expected after the exceptionally rapid rise in production that took place in virtually all the industrial countries during 1963. It is probably unavoidable that from time to time countries will find it necessary to introduce temporary measures of restraint to maintain internal and external stability. Indeed, some progress was made in 1964 in containing upward pressures on prices and wages where these had been excessive.

Although the slowdown continued in some countries in Europe in the early part of 1965, there are some grounds for belief that the pause in expansion may be only temporary. Expansion appears to be continuing at a substantial rate in several other countries in Europe, particularly in Germany, and in the United States and Canada, while the change in direction of monetary policies in Japan augurs a new upswing in that country. But the substantial enlargement of the world payments imbalance that took place in the course of 1964 imparted considerable uncertainty to the otherwise moderately favorable outlook for 1965.

International Payments

At the beginning of 1964, a reasonable degree of stability of international transactions prevailed. The balance of payments of the United States was close to equilibrium for the first time since the trough of the 1961 recession, even though the U.S. economy, after three years of continued growth, was still expanding at a substantial rate. The European Economic Community (EEC), which had been in persistent surplus for many years, also appeared to be close to equilibrium in its transactions with the rest of the world, even though there were considerable imbalances in countries within the area; these imbalances were sharply reduced early in the year. Lastly, the primary producing countries generally found themselves in improved balance of payments positions as a result of a rapid rise in their export earnings. But this pattern of relative stability was not maintained; 1964 was marked by a major deterioration in the balance of payments of the United Kingdom and the re-emergence of a sizable deficit in the United States and of a large over-all surplus in the EEC. In the last-mentioned area, the radical improvement in the Italian balance of payments was a most important factor. At the same time, the surplus position of the primary producing countries as a group was sharply reduced, and the balances of payments of many individual developing countries showed signs of strain. Thus, among the industrial countries, deficits again became concentrated in the two main reserve centers and surpluses in the European continent. Simultaneously, the gradual deterioration in the positions of primary producing countries, which hold a large proportion of their reserves in dollars and sterling, threatened to add to the pressures on the two reserve centers arising from their own balances of payments.

The deficits of the United Kingdom and the United States arose from rather different causes. In the United Kingdom, the deficit was for the most part due to a deteriorating current account position, associated with a rise in domestic demand, which had been stimulated by earlier fiscal and monetary measures; the rise in exports was less than in most other industrial countries and was insufficient to make up for the sharp rise in imports. In 1964, a large deficit on current account was augmented by a larger-than-usual net outflow of long-term capital. During most of the year, the deficit on current and long-term capital account was running at an annual rate of more than \$2 billion (equivalent to about two thirds of U.K. reserves at the beginning of the year). In the months to September, however, this deficit was largely offset by an inflow of short-term capital, and some assistance (mainly in August and September) from foreign central banks; reserves did not change much. In October, when a new Government had taken office, a program for dealing with the deficit problem was announced, including a temporary surcharge on imports of 15 per cent (lowered to 10 per cent in April 1965) and a system of rebates of tax on exports, averaging 1.9 per cent of their value. At that time, however, confidence in sterling was rapidly diminishing and, even though the Bank of England raised its discount rate to 7 per cent in November, a sharp reversal of the inflow of short-term capital, superimposed on the basic deficit, raised the over-all deficit to a record level in the fourth quarter. This created a serious crisis which was only overcome after it was announced that further international support for sterling, totaling \$3 billion, had been organized in the form of commitments to assistance by 11 countries and the Bank for International Settlements. In December, the United Kingdom drew \$1 billion from the Fund. The Fund obtained \$405 million of this amount by borrowing under the General Arrangements to Borrow, which were activated for the first time, and $250 million by the sale of gold. However, though there was a major improvement in the United Kingdom's current account position, its balance of payments remained under pressure in the early months of 1965 as outflows of capital continued. The budget introduced in April, which was again aimed at restraining domestic demand, and measures introduced to stem the outflow of capital helped, however, toward restoring confidence in sterling. In May, the United Kingdom made a second drawing from the Fund—$1,400 million, of which $525 million was obtained by the Fund under the General Arrangements to Borrow and $400 million by the sale of gold.

In contrast to the situation in the United Kingdom, the deterioration in the over-all U.S. balance of payments occurred in spite of a record surplus on goods and services account. The rise in the over-all deficit after the first quarter of 1964 was entirely attributable to private capital movements. During the first half of 1963, there had been a sharp rise in the outflow of U.S. portfolio capital, to which the U.S. authorities had responded by proposing in July the imposition of an Interest Equalization Tax applicable to the purchase of outstanding foreign securities and, with certain exceptions, to new issues. A subsequent reduction in the outflow of U.S. capital contributed to an improvement in the over-all balance of payments culminating in the first quarter of 1964. After that quarter there was a new upsurge in the outflow of U.S. capital, a contributory factor being a continuance of moderately expansionary policies in the United States in combination with policies of financial restraint in a number of the other industrial countries. The rise in the capital outflow included a large increase in bank loans, which were not covered by the proposed Interest Equalization Tax, enacted in September. The outflow increased during the last quarter of 1964, when there was a temporary rise in new issues, mainly of Canadian securities, following confirmation of the proposed exemption of these securities from the Tax. A further factor was the deferment, because of the sterling crisis, of payments by the United Kingdom of interest and amortization on its postwar loans, due in December.

The large increase in the outflow of U.S. capital in 1964 was accompanied by an increase in the inflow of foreign private liquid funds, which reduced the pressure on U.S. reserves and, together with some other factors, helped to minimize the outflow of gold. Calculations of the U.S. deficit differ—and for 1964 more than for any other recent year—mainly because some definitions do, and some do not, allow for this inflow of liquid funds. According to the concept generally used by the Fund for the analysis of world payments problems, which makes such an allowance, the U.S. deficit in the last quarter of 1964, on a seasonally adjusted basis, was about the same as the quarterly average for 1963, although the deficit for 1964 as a whole was considerably smaller than that for 1963. These calculations are lower than those based on the conventional concepts of the U.S. Government. It is, of course, impossible to express in a single figure all the varying facets of strength and weakness of the U.S. balance of payments, but whatever viewpoint is adopted there is no doubt that the re-emergence of a U.S. deficit at a substantial rate after the first quarter of 1964—following six years of large deficits—created a very difficult situation.

During the early months of 1965, pressures on the U.S. balance of payments were augmented by a dock strike, while a further outflow of capital appeared to be stimulated by an expectation that additional measures to reduce the outflow of capital would soon be introduced. In February, the U.S. Government announced a new and comprehensive program to deal with the balance of payments problem, the main features of which were a broadening of the scope of the Interest Equalization Tax and the enlistment of the voluntary cooperation of banks and other financial and nonfinancial corporations in reducing bank and other loans to foreigners and the placing of liquid funds and direct investment abroad. In formulating this program, an attempt was made to avoid as far as possible discouraging the outflow of capital to developing countries and to other countries (such as the United Kingdom), whose balances of payments were relatively weak. Special treatment was also accorded to Canada and Japan, which are heavily dependent on the U.S. capital market.

Early indications of the operation of this program suggest that it is being reasonably successful, although the precise nature of the market reactions and policy responses which it may induce in other countries cannot yet be known. While control of the direction of its impact is administratively difficult, the intention is that the impact should fall mainly on continental Europe as the major surplus area. In those countries where inflows of capital from the United States have added to inflationary pressures, a reduction in these inflows should enable the authorities to relax somewhat the restrictive policies that they have applied to contain these pressures, where this can be done without endangering internal stability. Such relaxations should help to reduce the repercussions on the U. S. balance of payments of the market reactions and policy responses referred to above. These repercussions could still be important, however, to the extent that the initial impact falls on countries in weak balance of payments positions.

Meanwhile, the normal processes of adjustment of underlying current account positions have continued. Costs and prices in the European area again rose in 1964 in relation to those in the United States. The U.S. current account position continued strong through the year, and the rise in the combined current surplus of the EEC countries in the second half of the year appeared to be attributable mainly to a slowdown in economic activity in certain countries, and thus likely to be of a temporary character. Indeed, one of the interesting aspects of the balance of payments situation late in 1964 was that, in contrast to the typical situation some years ago, the major surplus positions were not accompanied by excess demand, but by relative slack in the domestic economies of the countries concerned. Although these surplus countries remain subject to pressure on prices and wages—a fact that has to be taken into account—the slack in their economies should facilitate the adoption of policies that would assist in the process of international adjustment without damage to their internal stability.

As discussed in the next chapter, attitudes toward the role of capital movements in international payments have recently changed considerably. The large outflows of capital from the United States, mainly toward the other industrial countries—and in particular their resumption in 1964 at a higher rate than ever before in spite of the introduction of the Interest Equalization Tax—made it apparent that, for the time being, market forces alone would not bring about a pattern of capital movements consistent with balance of payments equilibrium among the major industrial countries. The past year has seen increased interference with the free movements of capital through measures of taxation, direct controls, and voluntary programs. While these programs raise important issues, they should in present circumstances assist in reducing the imbalance in international transactions. At the same time, an effort has been made to avoid undesirable repercussions on the balances of payments of the developing countries that might tend to slow down their rate of growth.

Primary Producing Countries

For the primary producing countries 1964 was, in general, a good year. On the average, prices of primary products exceeded the 1963 level by 5 per cent, and they were higher than they had been in any of the last eight years. However, prices for manufactured products also rose, and the terms of trade of the primary producing countries as a group were, on the average, only slightly more favorable than in 1963; they appeared to be worsening during the latter part of the year. In general, the experience of the more industrialized members of the group continued to be much more favorable than that of the less developed countries; the terms of trade of the former were, on the average, about 13 per cent higher than in 1958, whereas those of the latter had deteriorated slightly since that year.

The increase in the prices for primary products in general was accompanied by a rise in the volume of trade, and the rise of about 10 per cent from 1963 to 1964 in the export receipts of the primary producing countries was the highest recorded in a decade. Foreign aid remained at much the same level as in 1963, while the inflow of private capital expanded somewhat, and there was a substantial increase in the imports of the primary producing countries. Although the more industrialized members of the group increased their imports much more than the less developed countries, nevertheless the latter experienced the largest rise in several years in the volume of imports. As a result, the aggregate balance of payments surplus of the primary producing countries, which had been quite large in 1963, was reduced considerably in the course of 1964. The more advanced members continued to be in aggregate surplus through the year, but the less developed countries incurred a small deficit in the second half. In many countries, signs of increasing strains were appearing toward the end of the year.

The prices for metals and minerals, which during 1964 had shown the most pronounced increase of any primary product prices, continued to rise during the early months of 1965. The prices of most other primary products remained comparatively stable during most of 1964 at the relatively high levels reached in the early months, but they tended to weaken for a brief period at the end of the year. In general, they recovered slightly in the early months of 1965. Nevertheless, the international demand situation made it doubtful that the value of the exports of these products would continue to rise at the same rate during 1965 as in the preceding two years. Since the economic growth of developing countries depends largely on a sustained and adequate rise in the purchasing power of their exports, any weakening of their trading position would give new urgency to international measures to improve their export earnings, including reinforcing their access to markets in the industrial countries. This is a matter to which the Fund has given considerable attention over the years. In the course of 1964, the United Nations Trade and Development Board was established for the continuous study of the trade and development problems of the developing countries. The Fund has declared its intention to work with the new United Nations organs being established for this purpose, as it has for a long time done with other international agencies concerned with international trade problems and the special problems of the developing countries.

At the United Nations Conference on Trade and Development (UNCTAD) in 1964, certain recommendations were adopted under the heading "Study of Measures Related to the Compensatory Credit System of the International Monetary Fund." Some of these recommendations were addressed to members of the Fund rather than to the Fund itself, but all of them are being kept under consideration in connection with the continuing review of the still comparatively untried compensatory financing facility.[1] This facility was set up after a long period of study; thus far, evidence as to how it works has been scanty, thanks to the generally favorable export experience of the developing countries. Indeed, during the past fiscal year the Fund did not receive any requests for drawings under its compensatory financing facility; before that, only two countries had made use of it. This situation cannot in the nature of things be expected to continue for long, and another compensatory drawing has been made recently. As more experience is gained, it will become easier to form conclusions as to the desirability of effecting reforms in the present arrangements. The Fund is also cooperating with the IBRD in its current study of proposals to supplement the Fund's compensatory financing facility, which has been initiated by another resolution of the UNCTAD.

The balance of payments positions of the primary producing countries which prevailed during most of the past year were such that comparatively few of these countries made use of the Fund's resources. Drawings by these countries during 1964 were the smallest for five years and were exceeded by repayments. In the early months of 1965, however, their drawings rose substantially, and several new stand-by arrangements with nonindustrialized countries were made, including one for $200 million with India and one for $125 million with Brazil.

A cause of strain in the payments positions of the developing countries that has recently become significant arises from their increasing international debt burden. Expenditures for the servicing of foreign debt take a large and growing share of the export earnings of many of these countries, and it has become a matter of urgency to prevent a further rise in the burden of debt service. Some countries with heavy debt burdens have asked the Fund to assist, in an advisory capacity, in their negotiations for a rescheduling of debt; this aspect of the Fund's activity is reviewed in some detail elsewhere in this Report. In the Fund's consultations, therefore, increasing emphasis is being placed on the implications for the balance of payments prospects of member countries of their debtor positions, on long-term as well as short-term account. The Fund is also taking steps to improve its statistical reporting of indebtedness payable in the near future, in order to be able to

[1] The facility was described in *Annual Report, 1963*, pages 196-99. See also *Selected Decisions of the Executive Directors and Selected Documents* (third issue, Washington, January 1965, hereafter cited as *Selected Decisions*), pages 40-43.

be of more effective assistance to debtor and creditor countries alike. On all these problems, the Fund is working in close contact with the IBRD.

In several other directions, the Fund is expanding the services that it renders to the developing countries. The new Central Bank Service has been engaged on a considerable scale in advising on legislative proposals for establishing new central banks in newly independent countries and on the reorganization and administration of existing institutions. In addition, the panel of central bank experts that the Service has organized has provided executive staff for central banks operated by several of the Fund's members, and requests for such experts are increasing in number. The Fund is also giving, through its Fiscal Affairs Department, advice and technical assistance on taxation and fiscal administration, and is organizing a panel of fiscal experts, in order to be able to supply resident advisors on the request of member countries. By thus assisting member countries to strengthen the instruments of monetary and fiscal control, the Fund actively supports their efforts to promote economic growth in a favorable climate of monetary stability.

Countries' Reserves and International Liquidity

The increase in world reserves—apart from those of the Sino-Soviet area—in 1963 was the highest figure in any year since World War II, $3.4 billion. In 1964, the increase was some $0.9 billion less, at $2.5 billion, the decline being due mainly to a reduction in the rate of accumulation of dollars in the reserves of other countries, and to increased gold hoarding. In the first quarter of 1965, international reserves fell by about $800 million. Contributory factors appear to have been conversion of existing foreign exchange balances into gold by certain countries and continued private gold hoarding on a large scale.

The major event during 1964/65 in the field of international liquidity was the adoption by the Board of Governors of the Fund of two resolutions submitted to them by the Executive Directors for increasing Fund members' quotas. These resolutions (reproduced in Appendix I, p. 124) provided for a general increase of 25 per cent of members' quotas, together with additional increases for 16 countries whose quotas were considered to be out of line as a result of their recent economic development. If all the proposed increases become effective, total quotas in the Fund will rise from the current figure of about $16 billion to about $21 billion. This will add substantially to the conditional liquidity available to Fund members. The Executive Directors also decided to adopt policies and procedures designed to prevent gold subscriptions from reducing unduly the amount of reserves available to individual member countries, and in addition to mitigate the impact on the gold stock of the two major reserve centers of the subscriptions of other members.

Another noteworthy event was the activation of the General Arrangements to Borrow in connection with the two drawings by the United Kingdom in December 1964 and May 1965. The activation of the Arrangements not only was a demonstration of their usefulness but also led to the creation by the Fund of reserve assets in a new form as eight industrial countries acquired loan claims on the Fund to an amount of $930 million.

Continuing studies of international liquidity and of the functioning of the international monetary system are being conducted both by the Fund and by the Group of Ten. While there is wide agreement that there is no urgent need for additional international liquidity, the situation could alter if the United States succeeds in its program to eliminate its payments deficit. In that event, the environment in which international payments have taken place for more than a decade would be fundamentally changed. The rest of the world would, after many years, cease to run a large aggregate balance of payments surplus. Further increases in international reserves would be limited largely to the amount added to world monetary gold holdings. In the absence of deliberate international action to increase international liquidity, this change in the environment of international payments would reduce the impact which, in past years, has been exercised by the annual additions to world reserves. In these circumstances, it is generally recognized as important that consideration should continue to be given to the twin problems of international liquidity and the workings of the international monetary system. These questions, including the contribution which the Fund can make toward their solution, are discussed in Chapter 2.

Chapter 2

The International Monetary System and International Liquidity

Characteristics of the System

IN recent years, there has been increasing discussion in official, financial, and academic circles of the present international monetary system. This system comprises a spectrum of customary institutional and legal arrangements which govern the conduct of international economic transactions, the methods of financing deficits and surpluses in international payments, and the manner in which countries are expected to respond to such deficits and surpluses.

In its widest sense, the international monetary system includes the broad network of banking and commercial practices through which day-to-day international transactions are undertaken. The pricing of international shipments, the extension of credit, and the settlement of accounts take place in terms of many currencies. Mainly, these are the currencies of Western Europe and the United States, and more particularly, within that group, the major "trading currencies," i.e., the U.S. dollar, the pound sterling, and the French franc.

The predominance of the currencies of major trading countries is not surprising. A country with a very large world trade will develop a network of banking arrangements necessary for conducting that trade. The facilities and experience offered by these arrangements are then available to transact not only the trade and related payments between that country and its trading partners, but also those between other countries. The fact that a large trading country is also likely to have a well-established money market, and to be an important source of capital, further extends the use of its currency. For these and other reasons, such a country is likely to have long-established relationships with many other countries, causing them to look to it as the center of their own international financial arrangements. In a basic sense, therefore, the international monetary system tends to be founded on the currencies of a few countries which loom large in the total trade of the system.

In a narrower sense, the international monetary system is the complex of international rules and understandings which have evolved in an effort to ensure, by international agreement, a fair and efficient method of conducting international transactions. In this sense, the present system of international cooperation and consultation, which arose to a large extent from the 1944 Bretton Woods Conference, is in sharp contrast to that of the interwar period, particularly the 1930's, when countries pursued their financial policies with little regard for, and little understanding of, the effects that these policies might have on other countries.

The present system comprises, to begin with, the provisions of the Articles of Agreement of the Fund, which are designed to foster the interconvertibility of currencies. It includes the par value system, under which a country is expected to maintain a fixed value for its currency relative to gold and to other currencies—alteration of the value being reserved to circumstances of fundamental disequilibrium and requiring consultation with the Fund and, in most cases, the Fund's concurrence. It comprises also those provisions of the Articles of Agreement of the Fund and of the General Agreement on Tariffs and Trade under which restrictions on current payments and on trade are generally allowable only in situations of balance of payments difficulty and are subjected to international regulation. In addition, the concept of the international monetary system embraces all those *de facto* practical arrangements which give life and reality to the legal provisions. For example, the principal link between currencies and gold is provided by the fact that the United States freely buys gold from and sells gold to monetary authorities, at fixed prices, for the settlement of international transactions; moreover, the principal industrial countries act together through the Gold

Pool to keep the price of gold close to par on the free market. All the main industrial countries other than the United States, and many other countries as well, stabilize their rates of exchange by buying and selling dollars on the exchange market, while a number of other countries achieve the same result by pegging on sterling or on the French franc. Although under the Fund Agreement countries are virtually free from obligations with respect to the control of capital flows, there has been a fairly widespread *de facto* liberalization of capital movements by the industrial countries.

Finally, the international monetary system covers the arrangements under which external reserves are held. At the present time, international reserves comprise not only gold but also such currencies as the dollar, sterling, and the French franc, gold tranche positions[1] in the Fund, and claims resulting from loans made to the Fund under the General Arrangements to Borrow. Beyond these reserves, countries have access to the drawing facilities in the Fund in the credit tranches; these facilities, which are made available on condition that the drawing country maintains or adopts policies calculated to correct in due time the payments deficit in question, constitute "conditional" liquidity. In addition, there has been built up in recent years a network of bilateral mutual credit arrangements between the United States and a number of major industrial countries, under which each participant can draw on its partner for short-term accommodation in the form of a covered "swap." Similar arrangements have been made on a number of occasions between the United Kingdom and other industrial countries.

Reserves and other forms of international liquidity make it possible for countries to finance their balance of payments deficits; and the volume, distribution, and manner in which these reserves are made available have obviously an important bearing on that aspect of the international monetary system which is concerned with the adjustment of such disequilibria.

The system as described thus combines two features that are complementary in character: the financing of imbalances and the elimination of imbalances. The task of managing the international system—which is an individual and common responsibility of all countries concerned—is, in a large measure, to strike a balance between these two features, and this has also necessarily been the primary and crucial task of the Fund as the international organization at the center of the system. It should be emphasized that the task can be lightened, and the performance of the system improved, insofar as countries see to it that major payments disturbances do not arise in the first place and are willing to cooperate to that end.

The task of international monetary management would be simpler if the objective were merely to finance payments imbalances, or, alternatively, to ensure that any disturbances in balance of payments equilibria were eliminated as quickly as possible. But it is not sufficient that deficits be financed; financing which is excessive in amount or in duration may constitute a distortion in the flow of real resources that should be avoided. Nor is it enough that international payments should be brought into balance without regard to the measures by which this is accomplished. Practically speaking, the aim must be the achievement of balance with the least possible sacrifice of the generally accepted objectives of economic policy, including full employment, an adequate and sustained rate of growth, maintenance of reasonable price stability, and the maximum degree of freedom in current international transactions. It is also important that distortions in the international flow of capital and financing be avoided.

In the world of today, national authorities place a higher priority than in earlier times on achieving specific objectives in the internal economy and are more willing to adopt economic policies to this end. Public understanding that marked unemployment and economic stagnation need not be suffered as conditions beyond the control of man is one of the most potent forces of the modern world. It is derived from, and it has stimulated, the development of techniques to influence the internal monetary situation and, beyond it, the national

[1] A member's gold tranche position is measured by the extent to which the Fund's holdings of the member's currency falls short of its quota. The policies governing drawings in the gold tranche are those set forth in Executive Directors' 1952 Decision on Use of Fund's Resources and Repurchases (Decision No. 102-(52/11); see *Selected Decisions*, pp. 21-24), and in the 1964 Decision on Procedure for Drawings in the Gold Tranche (see Appendix I, p. 123 and *Selected Decisions*, p. 49) under which the execution of requests for such drawings is expedited. All references to gold tranche drawings in the present Report should be understood in the light of these decisions.

economy. The result has been that high employment and sustained economic growth have been established among the social goals that countries resolutely pursue, and every government seeks to equip itself with the tools of monetary and economic policy which will allow it to meet those goals. Countries reject the concept, implied in the gold standard, that deflation and economic stagnation, or inflation and overheating of the economy, must automatically be accepted in the interests of external equilibrium; and in many countries, the most pressing task of national financial authorities is to accommodate the public's demands for high employment, economic growth, and price stability while maintaining external balance. Within any context of monetary and economic management, circumstances will arise in which countries, particularly when they suffer balance of payments disequilibria of a persistent character, will be faced with difficult choices among several external and internal policy objectives. Deficit countries that find themselves in such circumstances will need to choose whether to seek a solution to their problem in a degree of deflation or at least a slowing down of the rate of growth, in the adoption of measures to restrain payments for visible or invisible imports or capital transfers, in an adjustment in their exchange rate, or in some combination of these various broad policy approaches. Surplus countries may similarly find themselves forced to choose between inflationary pressure, the adoption of steps to restrain the inflow and promote an outflow of capital, and revaluation of their currencies.

Appraisal of the System

The international monetary system of today is thus a complex framework within which a very large number of countries seek to attain simultaneously, by a combination of policy instruments, an appropriate balance among a number of internal and external objectives. How well has the system served to attain these objectives?

Any attempt at answering this question and thus appraising the performance of the system must start from the realization that the development of national economies individually and of the world economy as a whole cannot properly be attributed only to the workings of the international monetary system, even in the broadest sense of that concept. The physical and human conditions under which production proceeds, as well as a country's own policies in many fields and the repercussions of the policies of other countries, have undoubtedly also had a major influence in determining the successes and failures of the past 20 years. These observations are particularly pertinent when one considers separately the experience of the developing countries and of the industrial countries; within each group there have been varying degrees of success. By and large, the developing countries, hampered by structural problems, notably the unsatisfactory development of their export earnings, have found it difficult to achieve simultaneously the goals of rapid growth and internal and external stability. Restrictions on imports and on payments for invisibles have often been resorted to, exchange rates have been depreciated, and internal imbalances have interfered with the expansion of the economy. This has, happily, not been the universal picture of the past 15 or 20 years, but it has been a common one. In recent years, however, there has been a growing awareness of the contribution which stability can make to sustained growth, and many developing countries are showing a determination to stabilize their internal and external economies to provide a sound basis for economic development.

The industrial countries have achieved a very high degree of success, as national governments have effectively pursued policies of full employment. Between 1950 and 1964, production in the industrial countries expanded at a rate of more than 5 per cent per annum, while the labor force grew by 1.3 per cent per annum; the large pockets of structural unemployment which at one time existed in most European countries, and which seemed likely to persist, were largely absorbed.

With respect to the objective of price stability, it must be noted that inflationary pressures continued to be felt, and the cost of living even in industrial countries increased over the same period by an average of 2.5 per cent per annum as countries found it difficult to reconcile full employment with price stability, a difficulty which is evoking attempts at establishing "incomes policies." Great progress has been made by Fund members in the removal of barriers to trade and in shifting from bilateral to multilateral payments, and all the major industrial countries have now accepted the convertibility obligations of Article VIII.

These on the whole impressive results have been achieved with rather slight use in the industrial countries of the instruments of balance of payments adjustment that were provided for at Bretton Woods. With the exception of one large-scale and widespread devaluation in 1949, which was a part of the postwar readjustment process, there have been relatively few changes in agreed par values. Similarly, the instrument of quantitative restriction on imports, which was provided for in the GATT as a facility for meeting balance of payments difficulties, has in fact been practically abandoned by countries once they have succeeded in dismantling controls. Payments restrictions have similarly lost importance as a means of balance of payments adjustment, particularly since the widespread acceptance of Article VIII in 1961. Finally, restrictions on capital payments, which were not placed under the requirement of Fund approval as were restrictions on current payments, have been subject to a substantial dismantling, although this trend has recently been checked.

On the other hand, the instrument of monetary policy—or, more generally, internal financial policy—has been applied for balance of payments purposes far more generally than might have been anticipated at the time of the Bretton Woods Conference. This has been attributable in part to certain favorable features in the general economic environment. For example, the persistence of high demand and expanding output has in many instances enabled countries to correct their incipient balance of payments deficits by measures that have not gone beyond bringing about a temporary pause in the expansion of their economies. This has been conspicuously true of the industrial countries as a group, but there are numerous examples of the effective application of domestic financial policy among less developed countries.

A number of features of the international economy have given rise to considerable re-examination in recent years; these include the role of capital movements and the scope for price adjustment. Questions have furthermore been raised about the working of the system in terms of the manner in which international liquidity is created and the forms in which it is held. These issues are taken up below.

Role of Capital Movements

The Articles of Agreement of the Fund left control over capital movements almost entirely to the discretion of national governments. Later on, a view that had been dominant before 1930 began to gain ground, viz., the view that freedom of capital movements was highly desirable in itself, and moreover that the movement of short-term funds might be regarded as an equilibrating factor in international payments which would diminish the need for reserves. In fact, the period since the late 1950's, especially after the main European currencies became convertible, has been characterized by a massive revival of capital movements among the industrial countries, in particular from the United States to Europe. The so-called Euro-dollar market has become a large pool of short-term funds connecting the money markets of many countries and influencing them all. Long-term capital markets have also become more closely linked through direct investment, through dollar loans issued in European markets, and through other channels. As a result of these new developments, a large measure of international financial integration has taken place in a short span of years, and this has had important effects on the conduct of internal financial policy. Before currencies were convertible, countries could to a considerable extent follow independent monetary policies: the resulting differences in interest rates and in the tightness of money had relatively little influence in inducing movements of capital. At present, however, the scope for independent monetary policy is becoming increasingly narrow. In these circumstances more emphasis must fall on fiscal policy, and countries have, to a larger extent than previously, to bring their monetary policies into line with those of each other. Where countries have found the mobility of capital to hamper excessively the use of monetary policy for domestic purposes, they have tended to intervene to limit in some degree the freedom of capital movements. Massive movements of long-term as well as short-term funds from the United States to European countries have played a part in the persistent balance of payments problems of the former, while accentuating the difficulties which some of the latter have experienced in containing existing inflationary pressures. More generally, capital movements have frequently played a disequilibrating, rather than an equilibrating role, especially at times when there were thought to be prospects of exchange appreciation or depreciation on the horizon.

As a reaction to these developments in capital movements, several surplus countries have limited inflows of foreign funds, and certain deficit countries have discouraged the outflow of funds by fiscal measures (such as the Interest Equalization Tax imposed in the United States) and by more direct formal and informal measures.

The unexpected magnitude in recent years of capital movements between the main industrial countries, and in particular the continued substantial dependence of the world in general on the U.S. money and capital markets, thus confront the international monetary system with a new area of problems, which are the more difficult to deal with since it is hard to judge the extent to which these capital movements are a response to a persistent and fundamentally sound tendency for capital to seek the highest real return, or how far speculative or other temporary factors or fiscal considerations play a role. Should these flows be considered as mere temporary phenomena and be financed by movements in reserves? Should it be expected that current account balances will be radically changed to accommodate them? Or should the flows in some way be limited by controls? There are no agreed answers to these questions, and it may take much study, discussion, and coordination of national policies to find a satisfactory practical solution.

Scope for Adjustment of Price Levels

Another element which, as has long been recognized, adds to the difficulties of managing the international monetary system is that changes in price levels cannot be counted upon as a quick or adequate equilibrating force between deficit and surplus countries. The social forces which are arrayed against deflation have been noted earlier. Modern conditions make it very difficult for deficit countries to force down their general price levels without giving rise to the danger of provoking substantial unemployment of labor and underutilization of plant. At best those countries may be able (as has the United States in the past few years) to maintain a fairly stable level of prices. On the other hand, there is an understandable feeling in surplus countries that any addition, through their payments surpluses, to inflationary pressures already present in their economies should be resisted. Thus, whether or not price adjustments played a large equilibrating role in the past, it is clear that in present circumstances large imbalances cannot be expected to be eliminated within a short period of time by reliance on differential price movements alone.

Role of Reserve Currencies

Currencies of the reserve centers form, next to gold, the largest component of countries' reserves. Any rise or fall in the holdings of such currencies tends to result in a rise or fall in the gross reserves of the world as a whole. It is sometimes contended that this component in the world reserves total affords reserve center countries an undue and exceptional facility for financing balance of payments deficits, that its magnitude is determined by factors that have little to do with the world's need for reserves, and that it constitutes an element of potential instability in the international financial system.

It is no doubt a fact that payments deficits and surpluses of reserve centers, being matched by corresponding surpluses and deficits of other countries, tend to be associated with rises and falls respectively in the value of currency reserves and hence of total reserves. So long as the center is strong and enjoys unquestioned confidence, some proportion of its balance of payments deficit may be met by an accumulation of liabilities to official foreign monetary holders. In the last six years as a whole, the United States has financed some 40 per cent of its deficit in this way, despite the growing awareness of the need to reduce this deficit. As far as the United Kingdom is concerned, however, outstanding sterling balances have tended to fluctuate without a clearly defined trend. Most of the financing of the U.K. deficits in the last decade has been provided by the Fund or, for very short periods, by special assistance from the monetary authorities of other countries. The ability of any reserve center to finance deficits by increasing its currency liabilities is in any event not without limit.

The gold exchange standard, however, involves more than the ability of a reserve center to finance its payments deficit. Reserve centers originated as places where the monetary authorities of other countries—for reasons of convenience, access to capital markets, etc.—decided to hold a substantial proportion of their reserves; and while reserve center countries have some advantages, they are also exposed to pressures when currency balances are transferred into other currencies or withdrawn in gold. These pressures may develop even when the reserve center is in external balance or in surplus. Whatever criticisms may have been expressed about the present system of reserve currencies, there has been no significant tendency for countries to transfer their reserves to potential new reserve centers; nor has there been any inclination on the part of any country whose currency might be thought of as an alternative reserve currency to welcome or to encourage any such development.

The practice of holding foreign exchange reserves, whatever its merits from the point of view of the reserve centers themselves, has the inevitable consequence that the supply of reserves comes to depend greatly on the balance of payments situation of reserve centers and the confidence in reserve currencies. It is important not to exaggerate the degree of instability that is likely to arise from this cause by looking at parallels drawn from earlier periods. The international monetary system has been managed much more effectively in the postwar than in the interwar period. Initial tendencies toward declines in reserves during the early postwar period were more than offset by massive aid financed by the main reserve center, the United States. During recent years, when the United States has been in deficit, the rate of reserve accumulation in other countries has deliberately been influenced by agreement on such specific devices as advance debt repayments and swaps. If the strengthening of the payments position of the United States that is now under way were to go so far as to threaten excessive pressure on other countries in general, there would be opportunities for corrective action on the U.S. balance of payments (e.g., by alteration or relaxation of measures to restrain dollar outflows from the United States) or on other countries' reserves (e.g., by a build-up of a larger U.S. position in the Fund and a possible accumulation of foreign currencies as part of the U.S. reserves). Nevertheless, these possibilities of ad hoc mitigation do not entirely destroy the validity of some of the criticisms made of the system; nor do they justify delay in exploring other ways in which it may be possible, as the need may arise in the future, to supplement the growth of reserves in a more deliberate manner.

Types of International Liquidity

The subject of international liquidity was dealt with at considerable length in Part II of last year's Annual Report, and some of its aspects can be dealt with more briefly here. As was there pointed out, a country's external or international liquidity represents all those resources to which its monetary authorities have access for the purpose of financing balance of payments deficits. If there is too much international liquidity in the world, some countries are likely to pay too little heed to possible deficits and hence to tend to engage in overexpansive financial policies. As a consequence of this, other countries may find that surpluses develop on an excessive scale because balance of payments financing is too easy and cheap. If there is too little international liquidity in the world, deficit countries will have too little time to adjust in a desirable way to the disequilibria which develop, and will be forced to adopt unduly restrictive financial policies as well as to impose restrictions on trade and capital movements. As a result, the growth in world production and trade may be hampered and the prices of primary products depressed.

To what extent these various consequences will ensue depends in part on the composition and distribution, as well as on the quantity, of the international liquidity available. In the Fund it has been found useful to distinguish between conditional liquidity, which is available to a country in the form of credit facilities subject to the adoption of satisfactory policies looking toward balance of payments adjustment, and unconditional liquidity or reserves which are more or less freely at the disposal of the country. The Fund itself is much the largest provider of conditional liquidity in the form of drawing rights under the quotas. In the interest of maintaining economic activity at a high level and keeping international trade as free as possible from restrictions, while at the same time countering inflationary pressures, the supply of this type of liquidity should be adequate to meet all legitimate needs. It is for this reason that the Articles of Agreement provide for the periodic review of countries' quotas in the Fund.

Ideally, countries' needs for additional liquidity could be met by adequate increases in conditional liquidity. In practice, however, countries do not appear to treat conditional and unconditional liquidity as interchangeable. For various reasons, countries which have adequate real resources like to have the major proportion of their external liquidity at their free disposal. Even if conditional liquidity were expanded on a substantial scale, some countries might attempt—in preference to relying on these facilities—to increase their own reserves by adopting balance of payments policies which, from a broad international point of view, would have to be regarded as undesirable.

Potential Need to Supplement Growth of Reserves

Since the publication of last year's Annual Report, the Fund has been devoting considerable attention to the problem of international liquidity. Its primary practical concern has, of course, been with the adaptation of conditional liquidity to world needs by way of the expansion of Fund quotas; this subject is dealt with at length in Chapter 4. In addition, however, it has been giving thought to the issues relating to possible inadequacies in the supply of world reserves, or unconditional liquidity, that might arise if the prospective trend of such reserves, based on the availability of monetary gold and any future increases (or decreases) in holdings of reserve currencies, were insufficient to satisfy the desire for owned reserves in an expanding economy. In fact, as indicated in Chapter 1, the current rate of expansion in reserves is substantially less than in the record year 1963, and it is unlikely to be of that order of magnitude in the immediate future. It is widely agreed that there is no urgent need for supplementing the volume of reserves, and that existing methods to create liquidity may suffice to meet the world's need for a time. Nevertheless, it is important that further progress be made toward an international consensus about the way in which the international monetary system should develop, including possible new techniques whereby the existing methods of reserve creation could be supplemented, if and when necessary, and to the extent required.

Deliberate Reserve Creation

During the past year, studies as to possible new methods of creating reserves have been made both within the Fund and among the countries participating in the General Arrangements to Borrow.

A basic assumption of these studies has been that no change will be made in the price of gold in terms of currencies in general. This assumption corresponds to the endorsement of the established price of gold as one of the bases of the present monetary system, expressed by the responsible authorities of the principal industrial countries as indicated in the Ministerial Statement of the Group of Ten,[2] an endorsement in which the Fund concurs. The arguments against a change in the price of gold, including the inequities it involves and the speculative movements to which it is likely to give rise, are well known and need not be repeated here. The progress made in international monetary cooperation since the 1930's should make it possible for the world to achieve a more deliberate control over the amount of reserves through international action and to avoid sudden changes in the relative value of different reserve media.

The studies mentioned above have focused mainly on the deliberate creation of reserves by collective international action in the light of an appraisal of the general need for reserves rather than on their creation in response to immediate needs of particular countries for balance of payments assistance. Compared with the existing mechanisms of reserve creation, this constitutes a new approach which raises a number of important issues, e.g., how to establish and measure general reserve needs, in what forms additional reserves should be made available, what role they

[2] Paris, August 1, 1964.

should play in the international payments system, in which ways they should be created, how they should be distributed initially, and what institutional provisions should be made to ensure proper management of their volume and functioning. The question also arises as to the way in which, if conditions warranted, reserves should be reduced.

All these questions require a great deal of further study from the point of view of objectives as well as techniques. This Report can do no more than discuss them in a preliminary and general way and indicate what could be done by the Fund. It does not attempt to provide definitive answers or present concrete proposals.

Criteria of General Reserve Needs

Appraisal of general reserve needs is not something that can be carried out on the basis of precise criteria. Resort to qualitative judgment is inescapable. In particular, no close relationship exists between these needs and such simple indices as the value of international transactions. In the exercise of such judgment, attention has to be focused primarily on the nature of the reactions, particularly in the sphere of national policies, which it appears appropriate to encourage or discourage in the interest of sound development of the world economy with a minimum of monetary disturbance. Some of the consequences, or symptoms, of excess or deficiency in international liquidity were discussed at page 14 above. In the light of this analysis, the following appear to be the main criteria on the basis of which consideration should be given to an increase—or, on rare occasions, a decrease—in international liquidity: whether, in circumstances in which countries' financial policies are likely to be influenced by the level of world reserves, it appears desirable on balance to enlarge the scope for an expansion of monetary demand or to influence countries in the direction of counterinflationary action; whether, on balance, exchange rates are under undue pressure, or needed adjustments in exchange rates are being unduly delayed; and whether there are widespread restrictions in international transactions, or widespread tendencies to speculative capital movements that an expansion in world reserves could to some extent relieve. Some of these conditions might, of course, call primarily for a change in the supply of conditional rather than unconditional liquidity, or for other changes in the techniques of international cooperation, but they are all relevant in some degree to the question of reserve needs.

Types of Reserve Creation

Reserves may be created directly between countries, either unilaterally (as when one country acquires a reserve currency for gold) or bilaterally (as when two countries make a reciprocal, i.e., swap, credit arrangement or carry out an actual swap transaction). Plans for systematic reserve creation, however, have usually involved action through the intermediacy of an international institution. It may be convenient to distinguish two main techniques through which such an institution can create reserve claims: (1) by extending unconditional borrowing rights or drawing facilities to countries, and (2) by creating reserve claims on itself in exchange for value received, usually in the form of claims on countries. These countries can be either (a) identical with or (b) to some extent different from the countries that acquire reserve claims on the institution. Possibility (a), which has been envisaged in certain of the plans that are under consideration, is equivalent to a multilateral swap transaction or an exchange of claims between each participating country and the institution. Possibility (b) may be illustrated by analogy with the operations of a domestic banking system, which by lending to one set of customers in due course creates deposit liabilities vis-à-vis a somewhat different set.

Transferability of Reserves: Direct and Indirect

In order that a borrowing right or asset may be suitable for inclusion in a country's official reserves, it must be available as needed to meet payments deficits; that is, it must be convertible virtually on demand into the currencies in which these deficits are incurred. One way to assure this is to transfer the reserve claim on the institution to another holder in exchange, e.g., for dollars or the currency of the purchaser. Another way is for the institution itself to convert or encash the reserve claim for needed currency. In this case, the reserve claim will, in effect, be transferable through the institution. This happens, for example, when a country with a gold tranche position in the Fund makes a drawing from the Fund—the position is transferred to the country whose currency is used.

If transferability, whether directly or through the institution, is to be ensured, countries must have certain obligations to accept transfer in the form of lines of credit or otherwise, although these obligations need not be unlimited. The nature of any limitations imposed on the acceptance of transfer will largely determine the usability of the reserve asset. For example, if countries undertake to accept transfer of the reserve asset in question only in a certain ratio to gold, or to gold and foreign exchange, then other countries will be able to use the asset to meet their payments deficits only in the specified ratio to gold, or to gold and foreign exchange, respectively. On the other hand, if the holder of the reserve claim is to be able to use it freely, other countries must be prepared to accept it freely. In practice, the more freely the reserve claim can be transferred at the will of the transferor, the more likely countries are to insist on a quantitative upper limit to their obligations to accept transfer.

The procedures that are at present applied with respect to the use and transfer of reserve positions in the Fund represent something intermediate between free transferability and a system under which such positions are held and transferred in a fixed proportion to other reserves. A member can draw on its gold tranche virtually at will on representation of a payments need. In regard to the currency drawn—and hence the country to which the reserve position is transferred—the drawing country consults the Fund, which strives to ensure an equitable distribution of reserve positions in the Fund in the light of the balance of payments and reserve positions of the countries whose currencies are considered for drawing. Over the long run, the reserve positions in the Fund of members whose currencies are suitable for drawing have, as a result of this arrangement, tended to approximate a uniform proportion of their total reserves. All this takes place within the framework of creditor limits set by the quotas and beyond these by commitments under the General Arrangements to Borrow.

Apart from these questions relating to the usability or liquidity of the newly created reserve claims, certain other attributes of these claims have importance, such as whether they enjoy a value-maintenance guarantee, whether they bear interest (or in the case of borrowing rights, whether their use costs interest), and what will happen to them in the event of liquidation of the scheme. These matters are important primarily as affecting the acceptability of the new reserve claims, but also because of their possible repercussions on countries' preferences between holding gold and holding reserve currencies.

Distribution of Initial Reserve Increases

One of the most important questions to be asked with respect to any scheme for creating reserves would be how the initial increase in reserves would be distributed among countries. If reserves were created in the form of automatic access to credit, the initial increase in reserves would accrue to the countries which received such access. If reserve creation resulted from a purchase of assets by the institution, the initial increase would accrue to the countries whose liabilities the institution acquired, not necessarily to those that financed the operation by acquiring the newly created liabilities of the institution. For example, if the two groups of countries were separate and did not overlap, the countries whose liabilities the institution acquired would obtain additional reserves (initially in the form of balances in the currencies of countries of the other group), while the latter, though they acquired reserve claims on the institution, would probably lose reserves in other forms as a result of conversion.

A number of important considerations would enter into the decision as to the allocation among countries of any additional reserves that were to be created.

Any scheme of reserve creation would have to involve criteria to determine what countries would participate in the distribution of reserves and in what proportions. The countries participating in the distribution would be affected both directly, by having larger reserves at their disposal, and indirectly, because of the effect of increased reserves on the policies of other countries, which, as a result of easier liquidity conditions, would be induced to pursue policies that would increase their import demand and/or would be more willing to export capital or give aid. Countries not participating would be affected only in this indirect manner.

Whatever the initial distribution of reserves, the bulk of them would probably gravitate sooner or later to countries with a high propensity to hold reserves, such as the industrial countries and certain primary producers. To the extent that the initial distribution of reserves was confined to countries with a strong tendency to hold reserves, the effect of reserve creation on balance of payments surpluses and deficits, i.e., on the movement of real resources among countries, would be minimized, apart from short-run fluctuations. Conversely, where reserves were distributed directly to less developed countries (which on the whole have a weak tendency to hold and accumulate reserves), the creation of reserves would also involve a long-term movement of real resources from the more developed to the less developed countries. An important question to be considered is whether a mechanism which involved such transfers of real resources would be desirable.

Finally, although the likelihood of a reduction in reserves or liquidation of a reserve scheme might be remote, all participants would have an interest in the quality of the assets backing the claims that were created.

Institutional Aspects

The foregoing discussion of various aspects of reserve creation has been conducted without reference to any specific institutional framework. The task of influencing the total level of world reserves could be carried out by a new institution or by an existing institution, such as the Fund. From a purely technical standpoint, it would in general be possible to attain through the Fund results similar to those that might be sought in other ways, although this might involve certain amendments of the Articles of Agreement.

It can reasonably be argued that a matter which is of concern to all countries should be handled in an institution that has been organized as an instrument of financial cooperation on a worldwide basis. This would, moreover, be one way of ensuring coordination between the function of providing individual countries with short-to-medium term balance of payments assistance on a conditional basis and any new function of influencing the aggregate supply of world reserves or unconditional liquidity.

Reserve Creation Through the Fund

As foreshadowed in last year's Annual Report, the Fund has, during the past year, continued to study technical aspects that could arise in connection with any plans for the creation of reserves in the Fund. The Fund staff has also participated in the studies carried on within the Study Group on the Creation of Reserve Assets established by the countries participating in the General Arrangements to Borrow.

The Executive Directors have given some preliminary consideration to technical aspects of possible methods of creating reserves in the Fund. The two main ways, although not necessarily the only ways, would be the following: (1) the extension of quasi-automatic drawing facilities beyond the gold tranche into some part of the credit tranches, and (2) an operation whereby the Fund simultaneously would obtain special assets and assume additional liabilities.

One way of raising members' reserve positions in the Fund would be by an Executive Board Decision on drawing policies under which the ratio of Fund currency holdings to quota up to which members can draw on a virtually automatic basis would be raised from the present 100 per cent to some higher percentage of quota. Such a Decision might apply to all members or only to such members as satisfied certain criteria.

It should be observed that unless the extension of automatic drawing facilities were accompanied by a corresponding extension of total drawing facilities, some contraction in the amount of conditional drawing facilities open to members would be involved. A mere substitution of unconditional for conditional drawing facilities would have disadvantages from the standpoint of the Fund's ability to influence its members in the direction of the adoption of appropriate balance of payments policies. The contraction of conditional facilities involved would also reduce the value of the reserve increase to members themselves. This would apply particularly with respect to drawing facilities in the first credit tranche, which are available to any member that is making reasonable efforts to cope with its balance of payments problems. These consequences could be averted by extending the limits for drawing facilities of each type by the same amount that the limits for automatic drawing facilities were extended.

A second approach to an increased role of the Fund in the creation of international liquidity would be through an enlargement of the balance sheet totals of the Fund. The Fund would acquire assets other than the ordinary currency holdings which determine the drawing facilities available to members. In order to finance this acquisition, it would expand its liabilities by borrowing in one form or another. From the asset side of the balance sheet, this form of reserve creation may be described as the acquisition by the Fund of "special assets"[3]; from the liability side, and referring to the form which the additionally created reserves take, it may be described as the creation of loan claims on the Fund.

The liabilities to be created would have to be suitable for incorporation in countries' reserves. The precise nature of these Fund liabilities (i.e., members' reserve assets) would have to be worked out, but they could include at least the following: (1) the facility of the asset to be encashed for useful currency at least as freely as gold tranche positions or, alternatively, to be transferred directly to other members; (2) a gold-value guarantee; (3) interest at a modest rate reflecting the gold value of the claim. It will be noted that claims under the General Arrangements to Borrow have these three characteristics.

Under either of the approaches to Fund reserve creation discussed above—the extension of automatism and the acquisition of special assets—reserves could be created on a more or less extensive basis, depending on the criteria to be applied for countries to be included.

Again, under either approach, suitable action would be required to enable the Fund, without impairing its own liquidity, to meet the additional claims on Fund resources (in the form of drawings or conversions) that would arise from the use of the reserves created.

Conclusion

The international monetary system as it exists today is sufficiently strong to allow of a calm and dispassionate consideration of the possibilities of amending and improving it. Even if there is no need for immediate action to create additional reserves, it is nonetheless important to consider well in advance the many problems of principle and technique that would present themselves if the necessity for such action should arise. The work that has been carried out in the Fund and, with the collaboration of the Fund's staff, elsewhere has prepared the way for further advance toward an international consensus regarding both the major objectives of liquidity policy and the broad nature of the techniques to achieve these objectives. The Executive Directors have not, at this stage, attempted to reach a common view on the merits of the various possibilities indicated above. They intend, however, to devote further attention to these matters in the coming year.

[3] The same concept was referred to as Fund "investment" in *Annual Report, 1964,* page 38.

Chapter 3

Some Problems of Developing Countries

Introduction

IN its relations with developing countries, as with other members, the Fund is guided primarily by a desire to implement the purposes outlined in the first of its Articles of Agreement, and in particular

> to facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy.

By far the greatest number of Fund transactions have been with countries which may be considered to be developing rather than developed, even though a small number of large drawings, such as those by the United Kingdom in 1956, 1961, 1964, and 1965, France in 1957 and 1958, Canada in 1962, Japan in 1953 and 1957, and the United States in 1964, have accounted for over half of the value of total Fund transactions. Since the large majority of the Fund's members are developing countries, most of its consultations are with them, and conducting relations with these countries is a major part of its day-to-day activities.

It is difficult to make generalizations regarding the problems of the developing countries. Many are primarily dependent on the export of a few commodities to provide the imports which account for a large part of their consumption and investment; others have already achieved a high degree of self-sufficiency. Some are faced with serious population pressures; others are able to absorb a fairly large number of immigrants. In many cases, their export products are subject to large price fluctuations, which make the determination of the prospective profitability of investment uncertain and the maintenance of balance of payments equilibrium difficult. Furthermore, most exporters of primary products are also importers of other primary products. When, as in 1964, the prices of some such products fall relatively to others, those countries that export the former and import the latter will suffer. In the field of financial policy, many of the developing countries have been able to achieve growth in an atmosphere of financial stability; for a few countries, inflation seems to be almost an endemic problem.

While the Fund is necessarily interested most directly in the financial problems of the developing countries, it recognizes that these account for only part of the real internal and external difficulties facing these nations. However, experience indicates that these difficulties are most likely to be successfully overcome when policy is directed toward the maintenance of internal and external financial equilibrium. Even if this stability is achieved, it will not necessarily guarantee that rapid progress is attained; monetary stability must be regarded as a prerequisite for sustained economic expansion, rather than as an objective in itself. Even the best of policies can only speed the achievement of potential progress.

In previous Annual Reports, a number of the financial problems facing developing countries have been discussed. In 1962, the relation between inflation and economic development was reviewed at some length; and in 1963, some of the trade and payments difficulties of the developing countries were discussed and methods to cope with them were considered. These are aspects of the more general financial problem facing developing countries.

This chapter deals with two other aspects of this general problem which are frequently encountered in developing countries, and with which the Fund is increasingly concerned. The first section of the chapter discusses briefly problems arising from structural weaknesses in countries' fiscal systems; the second reviews at greater length difficulties arising from excessive burdens of short-term foreign debt.

Fiscal Systems

The Problems

For some years past, the discussions which the Fund has had with countries planning stabilization programs have shown that budget deficits are a major problem in many such countries. Indeed, it may not be too much to say that these deficits are the most frequent cause of the balance of payments difficulties of countries seeking assistance from the Fund in support of stabilization programs.

Many developing countries are faced with rapidly growing populations and a need to improve living standards. Their aspirations have led them to undertake ambitious expenditure programs in order to accelerate the rate of economic growth and to provide more government services. These programs involve not only the expansion of public investment in transportation, power, sanitation, and water, but also higher expenditures on education, public welfare, and other services, to meet the rising expectations of the population. Once a government becomes committed to a high and rising level of expenditure, the curtailment of spending programs is politically difficult. At the same time, the revenue systems of most of the developing countries are not structurally capable of supplying a rapid increase in financial resources. In most such countries, these systems, and the tax rates, are inadequate to obtain the necessary growth in revenue and are generally not conducive to development. Moreover, they are often so complicated that a general increase in rates would most likely lead to further economic distortions and administrative difficulties, with little growth in revenue. Simplification and reorientation, together with judicious increases in appropriate rates, are what is required.

A further complicating factor is that the existing revenue systems are generally inelastic relative to economic growth. Basically, this inelasticity reflects the fact that taxation does not tap adequately the more dynamic sectors of the economy. A major cause of the inelasticity of the revenue systems has been the inevitably heavy dependence upon import and export duties. On the import side, these have been rendered comparatively sluggish by balance of payments limitations upon the growth of imports, by the fixed character of specific duties, and by the shift in the composition of imports toward capital goods and raw materials that generally carry lower duties or are even exempt from them. The prevalence of specific indirect taxes and of land taxes based on long outdated assessments also inhibits revenue growth.

The scope for borrowing by the public sector in the developing countries is quite limited. Usually, the capacity of the capital market in developing countries is exceedingly small and is limited more by the low level of income per capita than by the lack of institutions for channeling savings into productive employment. Some borrowing is possible from small savings—for example, post office savings and low-denomination government bonds—and from pension funds. Usually, however, internal borrowing by the public sector is mainly from the banking system. Since the scanty supply of financial savings through the banking system has to assist in financing the over-all requirements of the economy, only modest amounts can be obtained from this source if the private sector is to have adequate funds to meet its needs for growth. The total amount of external financing is limited by the over-all supply of such funds, by the shortage of projects suitable for such financing, and by balance of payments considerations. In particular, external credits with short repayment terms can lead and in many instances have led to serious balance of payments difficulties.

When internal borrowing (largely in the form of bank credit) leads to a primary monetary expansion beyond the needs of the economy, rising wages and other internal costs will impair the country's competitive position, stimulate imports, and result in a drain on foreign reserves. Such an inflationary situation tends to feed on itself. Wage and salary adjustments and subsidies to alleviate rising living costs increase budgetary expenditures. The revenue structure, in addition to being inelastic to growth, is usually not well designed to provide the necessary response to price increases. Specific import duties, where they exist, do not reflect changing values or composition of goods, and income and profits taxes are of minor importance. Indirect taxes on the internal economy are often specific, and property tax assessments lag behind changing values. Delays in payment of tax liabilities and inadequate administration and enforcement of the tax laws often worsen the situation.

The fiscal difficulties of many developing countries are aggravated by heavy dependence on the export of raw materials and sensitivity to fluctuations in prices due to the shifts in world supply and demand of a few basic commodities. Any decline in the prices of these items is soon reflected in falling government receipts from customs duties and internal taxes. Also, a country's financial problems may at times be intensified by disasters, such as floods, earthquakes, or prolonged droughts. The resulting loss of production not only precipitates a drop in taxable income but also entails greater expenditure for relief. However, weak fiscal systems can make the country's problems more difficult than they need be, and a strengthening of such systems can facilitate the solution.

The Fund has long aided its members in tackling the problems of inflation, and the establishment of the Fiscal Affairs Department will enable it to render greater technical assistance to countries seeking to improve tax structures, tax administration, and budget administration.

Steps to Strengthen Public Finances

Although taxable capacity is limited by low incomes and the difficulty of taxing the subsistence sector of the agricultural population, few countries do not have scope for increasing government revenues. Some countries have achieved impressive results. In India, for example, the ratio of taxes to national income was more than doubled in a 13-year period. The ratio had ranged between 4½ per cent and 6½ per cent, until the institution of the first development plan in 1951; by 1955-56 the tax ratio had risen to almost 8 per cent, and by 1963-64, it was pushed to over 13 per cent of national income. (The inclusion of municipal taxes would raise the level even more.) In Peru, the ratio of taxes to national income between 1952 and 1959 averaged approximately 9 per cent; in the succeeding four years, tax collections rose to 14 per cent of national income. In many other countries, the ratio has also been rising.

Countries attempting to deal with inflation and to bring their balance of payments under control have often had to adopt emergency fiscal measures which are helpful in the short run but which would be undesirable if long continued. These include such actions as the deferment of capital outlays and the imposition of surcharges on imports or foreign payments.

For the long run, improved budgeting, tax reform, and better administration are required.

Budgetary Planning and Control

The national budget, through which expenditures are authorized and taxes and other revenues are set, is the logical starting point for improving a country's finances. The budgetary process involves the establishment of priorities for expenditures for various public purposes, and these should be restrained within the over-all ability of the government to support them. The matching resources are made available from internal revenues, including taxes and other receipts and loans, or from loans from abroad. In order to ensure the efficient utilization of public funds, some countries have organized a budget office that has effective control over both planning and execution of budget expenditures, and have provided the office with adequate authority to keep expenditures within the limit of prospective resources.

It is also important to ensure the coordination of the operating policies and investment decisions of autonomous entities with the country's economic plans through appropriate forms of central review or control. This need was recently recognized in Mexico, and all decentralized agencies were required to submit their budgets to the executive for review and formal legislative approval. Improvements in accounting and reporting procedures are a necessarily related step for both expenditures and revenues, in order to provide the up-to-the-minute data which are essential for proper administrative control over expenditures.

Tax Reform

In recent years, many of the less developed countries have recognized the need to modernize tax systems so as to facilitate economic development and other social objectives. In parts of Latin America, for example, important tax reform programs have been undertaken which have greatly strengthened the revenues. Most of the recent reforms have been designed to introduce or to strengthen income taxes, to improve the incidence of import duties and internal sales taxes by higher rates on luxury and semiluxury goods, or to modify or eliminate tax barriers to new investment by various relief measures. Supplemental taxes on net wealth have been introduced in a few countries, and taxes on exports modified in others.

One of the most intractable problems frequently encountered is that of obtaining appropriate tax revenues from the agricultural sector. In many instances, this revenue is obtained through taxes on exports of important agricultural commodities and through duties on imports or excises and sales taxes on farmers' purchases. However, new techniques need to be developed to tap the predominantly subsistence sector and to widen the tax base by encouraging the conversion of production for subsistence into production for money income. Graduated personal taxes have proved useful in several African countries where land taxes are impracticable, although evasion is sometimes difficult to prevent. In other countries, improvements have been made in the assessment of land values and the collection of land taxes.

Tax reforms are commonly intended not only to increase revenues but to lessen interference with economic growth and to help to achieve a more even distribution of income and wealth. In some respects these objectives may conflict, so that compromises among them often become necessary.

Tax Administration

More and more countries are recognizing that the most effective means of strengthening revenue collection is often the improved enforcement and administration of existing taxes. Usually a long-range program is required, including reorganization of revenue departments, the hiring and training of suitable employees, and the payment of adequate salaries, as well as the introduction of modern techniques and controls to check evasion and irregularities. Greater voluntary compliance with the tax laws may be secured as taxpayers' confidence in the efficiency and fairness of the revenue administration grows.

To improve revenue administration, it may also be necessary to redesign and simplify the tax laws themselves. This may entail the consolidation of many separate taxes into a single integrated tax, as in Ecuador which recently combined 25 separate taxes on the export of bananas into a single unified rate of 20.4 per cent. Progress can also be made by the elimination of miscellaneous small taxes that are not justified by the cost of collection.

Pricing Policies of Public Enterprises

A major cause of government deficits has often been contributions to finance the operating deficits of public enterprises, which are frequently due to inadequate prices for the services provided. Railroads, other transportation, and electric utilities are common sources of drain on public funds; such a drain frequently results also from the production and distribution of consumer goods. These losses are often the result of conscious underpricing policies designed to provide subsidies to counter inflation. Many enterprises that cover operating expenses do not make adequate provision for the amortization of their initial capital investment or for expansion. Financial demands are often made on the government even by autonomous entities that are only loosely affiliated to it. The revenue structures of most developing countries are not strong enough to support both the increased expenditure required by an adequate development plan and the large financial contributions that the state enterprises often receive.

Some countries have reduced or eliminated the budgetary drain of public enterprises by placing them on a more efficiently operating basis. In Mexico, most of the state enterprises operate profitably. India has for many years been striving to operate its public enterprises so as to obtain surpluses for investment, and has been particularly successful with respect to the railways and some of the new industrial establishments. Serious attempts are also being made to improve the financial results of public enterprises in a number of other countries, including Argentina, Brazil, and Ceylon.

Debt Burdens and Debt Renegotiation

The Problem

In many instances, the strains arising from weak fiscal structures in developing countries have been eased temporarily by recourse to unduly large foreign credits, often for relatively short terms. In addition, in attempting to mitigate the immediate effects of inflation, governments have, in certain instances, acquiesced in the incurring of large short-term and medium-term debts by businesses and individuals, or, by granting import permits more freely than foreign exchange has been made available, have allowed the accumulation of large commercial debts to foreign suppliers. Another important factor in the emergence of heavy debt burdens has been that a shortage of long-term capital has induced governments to finance long-term development by short-term or medium-term borrowings.

In assessing the problems of development, there are many aspects of the question of debt burden. In one sense, debt servicing requirements need not be regarded as a burden, and even a rising level of debt service need not be a cause for concern. If the original external financing enables a country to build up its capital stock so that the gross flow of its total output is increased in a manner which permits it to improve its balance of payments by more than the associated debt service payments, it should be able to meet its obligations and still enjoy a rising standard of living. On the other hand, if the maturities of debts are out of line with the productivity of the investments this may be the source of difficulties. Even with reasonable agreement between debt maturities and investment productivity, problems of international transfers may arise, and, in any event, policies with regard to foreign borrowing must be shaped with a country's eventual capacity to repay constantly in mind.

In some respects, the problems related to a country's borrowing capacity are of more direct concern to creditor countries and to development institutions such as the IBRD than to the Fund. However, in a number of countries there are immediately pressing problems of financing relatively heavy debt burdens in the near future, and of controlling the incurrence of new indebtedness, which are of concern to both the Bank and the Fund.

Debt Repayment Schedules

A number of developing countries are presently faced with debt repayment schedules over the next few years which are very heavy compared with their potential earnings. While government debts with original maturities of 12 months or more are only a part of the total, some of the available data on this component provide an indication of the general magnitude of the short-term debt problem in a number of countries. Thus, the annual debt service requirements (payments of interest plus amortization of principal) on these public debts of 37 developing countries covered in Table 1 increased by over 250 per cent from 1956 to 1964. Not only have the government debts of some of these countries increased markedly in recent years, as indicated in Table 2, but the structure of these debts has altered so that relatively short-term debt forms a larger part of the total, as evidenced by the rise since 1956 in the immediate repayment requirements relative to the total outstanding

TABLE 1. THIRTY-SEVEN COUNTRIES[1]: ANNUAL SERVICE CHARGES ON MEDIUM-TERM AND LONG-TERM EXTERNAL PUBLIC DEBT, END OF YEAR, 1956-64

(In millions of U.S. dollars)

	1956	1957	1958	1959	1960	1961	1962	1963	1964
Latin America	455	575	779	848	1,049	1,084	1,280	1,271	1,442
South Asia and Middle East	95	162	186	217	284	298	378	445	485
East Asia	22	27	26	46	56	89	62	110	99
Africa	37	44	49	55	63	78	104	127	131
Southern Europe	71	50	60	127	253	202	174	307	341
Total	680	858	1,100	1,293	1,706	1,751	1,998	2,260	2,497

Sources: Data for 1956-62 are from Dragoslav Avramovic and associates, *Economic Growth and External Debt* (Baltimore, 1964), p. 107; those for 1963 and 1964 were prepared by the staff of the International Bank for Reconstruction and Development.

[1] *Latin America:* Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, Venezuela. *South Asia and Middle East:* India, Iran, Israel, Pakistan. *East Asia:* Burma, Ceylon, Malaya, Philippines, Thailand. *Africa:* Sudan, Ethiopia, Rhodesia and Nyasaland, Kenya, Tanganyika, Uganda. *Southern Europe:* Spain, Turkey, Yugoslavia. The debts covered are those with original maturity of one year or more.

debt, indicated in Table 3. In part, this increasing importance of short-term debt reflects the fact that sufficient long-term funds were not available to meet the desires of governments to finance capital development, or that there were no programs that could be financed in such a way, while foreign suppliers were willing to supply the equipment for this investment on relatively short-term credits, largely because their own governments guarantee a part of export drives. These some previous short-term capital receipts, and borrowings greater than repayments, with a consequent increasing obligation to meet outstanding commitments. Table 4 indicates that the short-term government and private liabilities of many developing countries to private U.S. lenders have been rising quite rapidly in recent years; and the United States has been only one of the sources of short-term finance, although the main one for Latin America.

TABLE 2. THIRTY-SEVEN COUNTRIES: MEDIUM-TERM AND LONG-TERM EXTERNAL PUBLIC DEBT, END OF YEAR, 1956-64

(In millions of U.S. dollars)

	1956	1957	1958	1959	1960	1961	1962	1963	1964
Latin America	4,277	4,921	5,711	5,816	6,573	7,615	8,913	9,531	10,594
South Asia and Middle East	1,398	1,756	2,527	2,811	3,322	3,914	5,073	6,549	8,575
East Asia	350	440	572	643	655	729	850	1,097	1,125
Africa	875	926	997	1,079	1,225	1,347	1,437	1,598	1,873
Southern Europe	1,079	1,082	1,304	1,517	1,482	1,695	1,958	2,416	2,637
Total	7,981	9,126	11,111	11,866	13,258	15,301	18,231	21,191	24,804

Sources: Data for 1956-62 are from Avramovic (cited in Table 1), p. 101; those for 1963-64 were prepared by the staff of the International Bank for Reconstruction and Development.

TABLE 3. THIRTY-SEVEN COUNTRIES: ANNUAL SERVICE CHARGES ON MEDIUM-TERM AND LONG-TERM EXTERNAL PUBLIC DEBT AS PERCENTAGES OF OUTSTANDING DEBTS, END OF YEAR, 1956-64

	1956	1957	1958	1959	1960	1961	1962	1963	1964
Latin America	10.64	11.68	13.64	14.58	15.96	14.24	14.36	13.33	13.61
South Asia and Middle East	6.79	9.22	7.36	7.72	8.55	7.61	7.45	6.79	5.66
East Asia	6.28	6.13	4.55	7.15	8.55	12.21	7.29	10.03	8.80
Africa	4.23	4.75	4.92	5.10	5.14	5.79	7.24	7.95	6.99
Southern Europe	6.58	4.62	4.60	8.37	17.07	11.91	8.89	12.71	12.93
Total	8.52	9.40	9.90	10.90	12.87	11.44	10.96	10.66	10.07

Source: Based on data in Tables 1 and 2. The data shown in Table 2 include lines of credit not yet drawn upon; on many of these, service charges are limited to a commitment fee. The percentages shown in Table 3 are therefore lower than those applying to that part of the debt which has in fact been used.

credits generally have maturity schedules that are not in line with the productivity schedules on the investment undertaken.

Data on other international indebtedness are more difficult to assemble, although short-term private and government borrowings are a large part of the total indebtedness. However, there can be no doubt that many developing countries have been receiving a rather continuous net inflow of short-term finance on government and private account, reflecting a "rolling-over" of

Irrespective of the origins of the problem, there can be no doubt that certain countries are now faced with very large external debt repayment schedules in comparison with their potential foreign exchange earnings. The rising trends of immediate debt service requirements related to export income are demonstrated in Chart 1 and the levels reached in a few selected countries in Latin America are shown in Chart 2. At present, a number of Fund members are faced with very heavy commitments.

TABLE 4. SHORT-TERM CLAIMS ON SELECTED COUNTRIES REPORTED BY U.S. BANKS AND NONFINANCIAL CONCERNS, END OF YEAR, 1960-64

(In millions of U.S. dollars)

	Total as of December 31				
	1960	1961	1962	1963	1964
Latin American Republics and other Western Hemisphere (excluding Canada)	1,650	1,810	1,989	2,157	2,746
Other primary product exporting countries	454	610	595	703	929

Source: Based on data in *Federal Reserve Bulletin.*

CHART 1. THIRTY-SEVEN COUNTRIES: EXTERNAL PUBLIC DEBT SERVICE AS PERCENTAGE OF EXPORTS, 1956-64

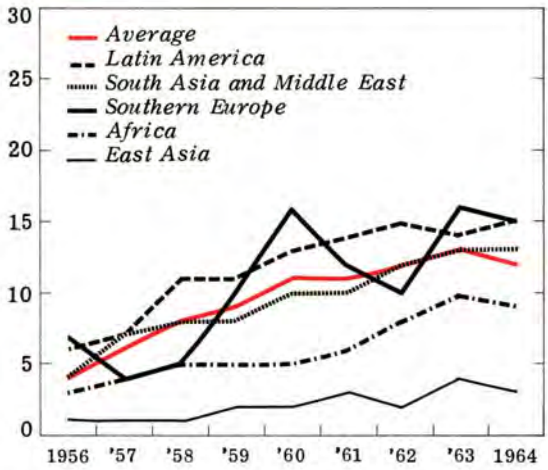
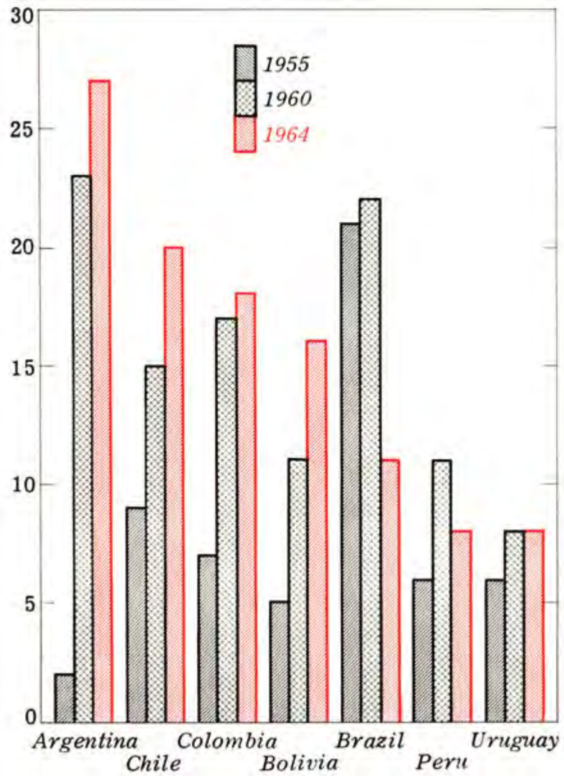


CHART 2. SEVEN LATIN AMERICAN COUNTRIES: EXTERNAL PUBLIC DEBT SERVICE AS PERCENTAGE OF EXPORTS, 1955, 1960, AND 1964



Renegotiation Possibilities

If a country's debt structure is such that it is faced with a heavy burden of repayment in the near future and much smaller payments in later years, it is possible that a postponement of some payments may convert an essentially intractable position into one where orderly repayments can be made. However, such rescheduling precludes further access to large amounts of short-term credit, if the rearrangement of debts is to be successful.

It must be recognized that in extreme cases countries are, in fact, faced with a choice between persistent default, reborrowing, unilateral moratoria (which only postpone the day of reckoning), and debt renegotiation to spread the burden over a number of years. In certain cases, the Fund has encouraged debtors and creditors to renegotiate debt contracts when such arrangements appeared appropriate to the particular circumstances that had developed. In these situations, the Fund has proceeded on the understanding that the debtors would adopt policies to make certain that the renegotiations would not merely constitute another postponement, new debts being accumulated during the period over which immediately pressing repayments are spread out.

The need for, and appropriateness of, debt renegotiation arises most frequently for countries trying to stabilize their economies after fairly prolonged periods of inflation. An essential part of many stabilization programs is the regularization of the countries' foreign debt positions. This regularization may require an abatement of the pressure of immediately payable accounts, so that all debts may be met in an orderly manner, while at the same time debt repayment does not absorb such a large part of a country's supply of foreign exchange that it is unable to pay for its essential external needs.

While debt renegotiation may be an essential component of an individual stabilization program, not only must such renegotiation involve an eventual complete repayment of the outstanding debts but it should be a rare event. If there is to be a flow of credit from the developed countries adequate to meet the needs of the developing countries, it is essential that the terms of debt contracts be taken seriously and that orderly relations between debtors and creditors be maintained. In a sense, there is a world-wide pool of international finance for development. The willingness of creditors to make funds available to this pool depends, in part, on their expectations that they will be repaid on the terms on which they lend. Failures by developing countries to meet obligations tend to undermine the element of confidence in international indebtedness on which borrowing by all developing countries ultimately depends. A formal renegotiation may serve to improve and gradually restore the credit of a country that is in serious difficulties in meeting its obligations, and enable the debtor to avoid a default, with its damaging effects on the international credit structure. Yet it may not suffice to restore the debtor's creditworthiness to the level at which it would have been if renegotiation had not been necessary. Hence the development of serious short-term indebtedness situations serves to weaken the forces working toward the raising of living standards in the developing nations. Consideration is being given in the Fund and elsewhere to ways in which it might be possible to forestall the emergence of excessive external debt burdens.

Present Practices in Debt Renegotiation

Some reasonably well-defined practices have developed in the debt negotiations that have taken place in recent years. These practices are by no means so firmly based that they may not be changed, but they take into account realities that will continue to be important.

Difficulties in arranging a new debt schedule sometimes arise from the nature of the debts under review. In some instances, they have been incurred without an adequate review of the original financing by the appropriate authorities in either the lending or the borrowing country. Some of these debts are the counterpart of not necessarily productive investments undertaken by individuals in the developing countries on the basis of credit freely extended by exporters in the industrial countries. As a result, the debts being refinanced may have arisen from investments which were not necessarily the most desirable or which may have been made at unduly high prices.

The technical prospects of refinancing may also involve difficulties. Even in creditor countries where the refinancing can be handled by an existing public institution without new appropriations, a considerable reluctance is sometimes shown by such an institution to have its funds used in this relatively unappealing manner.

Although the creditor countries have evidenced considerable sympathy for the problems of the debtors, they have, in general, emphasized their view that a debt renegotiation must be considered to be a very unusual event and that it is explicitly an appeal for creditor forbearance. The same concern of creditors has led to the application, where a second approach has been made by a debtor country, of more restrictive standards and more emphasis on avoiding a recurrence of the problem.

Refinancing has almost exclusively been on a national basis, the relief given by a creditor country being limited to payments on debts due to its own nationals. As there has been a considerable variation between countries in difficult debt situations, it has been widely felt that those which have taken the risks in order to gain export markets are also those which should bear the costs. Increasingly close attention has been paid to this matter because liberal relief or new credits by one country can be diverted to maintaining service on debts to others granting less liberal relief.

To ensure that the burden of refinancing is shared equitably among the creditors, they have attached great importance to unity of action, and it is usual for a rule to be adopted requiring all creditors to be treated alike. The multilateral agreements include a most-favored-nation clause, the purpose of which is to ensure that all debts within the scope of the agreement receive the same treatment. The bilateral agreements which are necessary to implement the general understandings reached at the major debt conferences are tailored to suit conditions and institutions in the individual creditor countries, and although they may have a varied form and timetable, the same basic principles, as agreed between the creditors, are observed.

Although uniformity of treatment has been sought, there has been reasonable understanding that debt arrangements cannot be negotiated with too large a group. No objection has been raised to the exclusion from the scope of a multilateral agreement of countries that are owed relatively small credits, since they hardly affect the basic problem. In fact, attention has been focused primarily on obtaining uniformity of treatment between major creditor countries rather than on individual country settlements. Particular concern for uniformity has arisen when the debt with countries in the Sino-Soviet bloc has been substantial.

The coverage of the debt to be renegotiated has usually been relatively restricted. Frequently it has been limited to debt arising from commercial arrears and suppliers' credits. In general, previously renegotiated debts and debts to international agencies have not been subject to further negotiation. Debts of central banks to private foreign commercial banks have also usually been outside any arrangement, although there has sometimes been parallel but less favorable refinancing in this area. Broadly speaking, the arrangements have been government to government—a situation facilitated by the widespread guaranteeing of export credits in most capital-exporting countries. Thus, the complexity of negotiations with large groups of private creditors has been avoided, and the damage to the credit standing of the debtor country has also been limited.

The problem of ensuring that the cost of refinancing is borne by those who openly assumed the risk has affected the coverage of some of the agreements. For example, in cases arising in the United States, where exporters have financed capital goods without any government guarantee, the U.S. authorities have generally wished to avoid giving a retroactive guarantee such as would be created if a government agency were to refinance these private debts. In the 1964 Brazilian renegotiation, the U.S. authorities did not undertake the refinancing of amounts due to private U.S. suppliers, and they urged the Brazilian Government to undertake such renegotiations direct.

The terms of refinancing have differed rather widely, but in general creditors appear to have been responsive to pleas to keep debt service down to a level considered reasonable in relation to the level of balance of payments receipts. They have been willing to accept a pause in payments in the early years when other debt service is unusually high, to be compensated for by increasing payments in later years. As most of the debts being renegotiated have been relatively short term, the renegotiated terms have not usually been beyond 10-15 years, and it has been appropriate that the level of payments arranged should have provided little leeway for accumulating new debts within reasonable limits of the debtor's capacity to repay. (This limitation generally has a deflationary effect because of the reduction in the inflow of capital.) Although there have been important exceptions, rescheduling has usually related only to principal payments; payments of interest have been expected to continue without refinancing.

Conditions for Success

The willingness of creditors to accept an appropriate rescheduling of debt service is related to the degree of assurance that the problem will not recur. In principle, the creditors acting collectively should be able to prevent this—they usually represent the major part of possible credit facilities—but in practice, cooperative arrangements without effective coordination have not been effective. Consequently, increased attention has been paid to the safeguards that can be provided through the cooperation of the Fund and the IBRD.

The need for cooperative action has been particularly important in connection with export credits from the countries supplying investment goods to the developing countries. Export credits serve a useful, and indeed a necessary, function as long as they are limited to the capacity of the importing country to make repayment in the short term or medium term. However, difficulties have arisen because of excessive resort to borrowing in the form of short-term export credits for the financing of the purchase of equipment for long-term investment uses. In part, the responsibility for many of these cases of over-indebtedness must be shared by the creditor countries, where the over-all national interest is rarely represented effectively. Too often, an exporter, on a plea that businesses in other countries might get contracts, is able to exert a very considerable pressure on his government to obtain an official guarantee. This is a difficult and delicate problem requiring cooperative action for its solution, to which the Fund and the IBRD are directing their attention.

On the debtor's side, the first decision in any debt renegotiation is to ask for relief. The timing of action to obtain such relief is important. Debt service builds up over time and may be accompanied by an accumulation of arrears of current payments. It is usually one product of excessive expenditures incurred as a result of domestic pressures which the financial authorities have not been able to resist. As long as these various pressures for expenditure are stronger than the countervailing desires for domestic stability, renegotiation is unlikely to be successful, for new debts will be incurred and the country will continue to be in difficulty. However, when the strain of the debt burden becomes sufficiently apparent, it serves to support efforts toward domestic stability, and, as a result, there may be sufficient backing from public opinion for responsible financial conduct. At such times, debt renegotiation may be desirable, and a successful renegotiation can strengthen the position of the authorities and provide them with an effective basis for requesting full control over all governmental foreign borrowing and for developing an integrated planning program.

The Role of the Fund

The Fund has never agreed to refinance debts directly, as such transactions would be outside its normal sphere of operations; its resources are available for the provision of relatively short-term assistance to meet balance of payments deficits. In most situations where debt renegotiation is appropriate, there is need for much longer-term financing than could be provided under the terms of the Fund's policy limiting the use of its resources to three to five years. Moreover, the debts are frequently large in relation to the member's quota, and their refinancing by the Fund would seriously limit the Fund's ability to meet genuinely short-term balance of payments difficulties. In many instances where debt renegotiation is only one aspect of a general stabilization program, financial assistance from the Fund to meet other aspects of the balance of payments readjustment problem is also a prerequisite for the program's success.

In the course of a debt renegotiation, the balance of payments position of the debtor is certain to be discussed. Although the debtor usually can present an exposition of its position, there is a decided advantage to both the debtor and the creditor if there can be an impartial presentation of the facts. The Fund is in a good position to provide such an analysis of the short-term and medium-term balance of payments prospects, while the IBRD is in a comparable position to assess longer-term development trends. The Fund provided this type of information on an informal basis as part of the negotiations with respect to the outstanding debts of Turkey in 1958-59, Brazil in 1961 and 1964, Argentina in 1962 and 1965, Liberia in 1963, Indonesia in 1963, and Chile in 1965. In the last-mentioned instance, the IBRD participated in the discussion.

The Fund has the opportunity to assist in preventing a recurrence of the need for debt renegotiation when a stand-by arrangement is being negotiated parallel to the debt refinancing, although it must be remembered that a stand-by arrangement lasts for not more than a year, whereas the repayment of a rearranged debt will take several years. Subject to this, mutual benefits can be derived from commitments given to the Fund under a stand-by arrangement, since if adequate measures to restore the payments balance are implemented, there can be some assurance that such problems as the accumulation of arrears will not recur. Safeguards against other methods of accumulating an undue amount of indebtedness—e.g., the excessive use of short-term and medium-term suppliers' credits—probably require the cooperation of a development agency such as the IBRD.

Another method, not connected with a program supported by a stand-by arrangement with the Fund, may be illustrated by the role that the Fund was asked to play in the negotiations with Brazil in 1964. At that time, the creditors and Brazil agreed to ask the Fund to be responsible for reporting to the creditors all information supplied by Brazil concerning the observance by Brazil of its new policy on the acceptance of suppliers' credits.

Conclusion

Operations with the developing countries have provided experience which demonstrates that the Fund and the IBRD can expect to be involved in the debt problems of these countries. In certain cases, the renegotiation of outstanding debts is an essential step toward a return to orderly international financial conditions. While the Fund recognizes that this step should be taken only in exceptional circumstances, it always stands ready to make its good offices available when appropriate. It has provided, and will continue to provide, the background information required to assess the need for debt rescheduling and to understand the magnitude of the problem facing debtors. Further, some stand-by arrangements include conditions intended to discourage excessive debt burden, including the acceptance of an unduly large amount of suppliers' credits. Finally, in its relations with member countries, the Fund is alert to the possibility (even if remote) of this problem emerging, and encourages the adoption of policies which will forestall the danger. Such encouragement lies within the Fund's competence as a source of short-term balance of payments credits. By supporting appropriate policies, it hopes to contribute to the maintenance of a system of international payments which will, among other objectives, assist in fostering an adequate flow of longer-term international finance for soundly based development programs.

Chapter 4

The Fund in 1964/65

THIS chapter reviews briefly the main features of the Fund's work in the past fiscal year. Further information, and statistical details, are given in a Supplementary Note on page 107-19.

Membership

The membership of the Fund remained at 102 during the year under review. With the increases in the quotas of certain members enumerated in Table 48 (p. 108), the aggregate of quotas on April 30, 1965 was $15,933.08 million. The Board of Governors approved terms and conditions for the admission to membership of Malawi, with a quota of $11.25 million, and Zambia, with a quota of $50 million.

The Fund was notified that the Republic of Tanganyika, a member country, had formed a union with Zanzibar, which had applied for membership in the Fund. The Executive Directors decided that the United Republic of Tanganyika and Zanzibar (subsequently renamed the United Republic of Tanzania) was a member of the Fund.

Article VIII

Nicaragua, with effect from July 20, 1964, Costa Rica, with effect from February 1, 1965, and Australia, with effect from July 1, 1965, accepted the obligations of Article VIII, Sections 2, 3, and 4, of the Fund Agreement, bringing to 27 the number of members which have rendered their currencies convertible under the Articles of Agreement. These countries are listed on page 107.

Executive Directors

The number of Executive Directors, appointed and elected, was increased to 20 at the time of the 10th Regular Election of Executive Directors, held during the Annual Meeting in Tokyo in September 1964. A list of the Executive Directors and Alternate Executive Directors and their voting power on April 30, 1965 is given in Appendix II, and changes in membership of the Executive Board during 1964-65 are shown in Appendix III.

Increase in Fund Resources

Since 1963, the Fund has expanded its studies of the international financial system and of the role of the Fund in this system. The Fund's views were set out in Chapters 3 and 4 of the Annual Report for 1964. That Report concluded (p. 36) that

> . . . there is a case for an increase in Fund quotas. The Fund should therefore proceed to an early examination of this question in detail. This examination should encompass the magnitude of a general and virtually uniform quota increase, the need for special additional increases for individual countries in the light of the considerations mentioned earlier in this chapter, the timing of such increases, and other relevant considerations. Under the Fund's normal practice, the Executive Directors would begin the quinquennial study of quotas at the end of this year [1964] with a view to reaching a conclusion by the end of 1965. There would be advantage in considering quotas as promptly as possible after the Annual Meeting of the Board of Governors [in Tokyo in September 1964].

At the Annual Meeting in September 1964, a large number of Governors spoke in favor of an increase in quotas. There was unanimous approval of the resolution "That the Executive Directors proceed to consider the question of adjusting the quotas of members of the Fund and at an early date submit an appropriate proposal to the Board of Governors."[1] The discussion made it clear, however, that there were differences of view among the Governors with respect to the size and urgency of a general increase of quotas, and with respect to the amount and num-

[1] Resolution No. 19-20; see *Summary Proceedings, Annual Meeting, 1964,* page 269.

ber of special quota adjustments. On the question of the general increase, some Governors expressed a preference for a moderate increase and others for a substantial one. The outcome of the discussion was a general feeling that an increase of the order of 25 per cent would be appropriate.

Proposals for Quota Increases

On February 26, 1965, the Executive Directors adopted a report entitled "Increases in Quotas of Fund Members: Fourth Quinquennial Review," to be submitted to the Board of Governors. The Report, reproduced in Appendix I, page 124, includes two Resolutions, the First proposing a general increase of 25 per cent, appropriately rounded, of all quotas, and the Second proposing special quota increases for 16 members. The First Resolution had to be voted on as a whole, but, for the Second Resolution, votes could be cast on all or each of the special quota increases. By March 31, 1965, both Resolutions had been adopted by the Governors by more than the required majority of four fifths of the total voting power.

Members may consent to the increases in their quotas at any time before September 25, 1965; this period may be extended by the Executive Directors. The increases will not become effective unless the Fund has determined that members having on February 26, 1965 two thirds of the total quotas have consented to them. If all members consent to the proposed quota increases, total quotas in the Fund will be increased to $21,049 million, exclusive of the increases under the Compensatory Financing Decision after February 26, 1965 which for the purposes of the Resolutions have been treated as if they had been submitted to the Governors before that date.

Size of Quota Increases

The First Resolution proposed that all quotas be increased by 25 per cent, rounded in accordance with the following formula:

> amounts below $500 million are to be rounded to the next higher multiple of $1 million; and
>
> amounts of $500 million or more are to be rounded to the next higher multiple of $5 million.

The revised quotas are shown in the table on page 129.

Under the Second Resolution, special quota increases were provided for 16 countries, as shown in Table 5.

A member consenting to a special increase under the Second Resolution is expected to request an increase in its subscription to the capital of the

TABLE 5. PROPOSED INCREASES IN QUOTAS, 1965; SPECIAL INCREASES

(In millions of U.S. dollars)

Member	Quota on Feb. 26, 1965	New Quota Under First Resolution	New Quota Under First and Second Resolutions
Austria	75	94	175
Canada	550	690	740
Finland	57	72	125
Germany, Federal Republic of	787.5	985	1,200
Greece	60	75	100
Iran	70	88	125
Ireland	45	57	80
Israel	50	63	90
Japan	500	625	725
Mexico	180	225	270
Norway	100	125	150
Philippines	75	94	110
South Africa	150	188	200
Spain	150	188	250
Sweden	150	188	225
Venezuela	150	188	250

Bank corresponding to the special part of its quota increase.

Gold Payments and Their Alleviation

Before the increase in a member's quota can become effective, the member is required to pay an additional subscription equal to the increase in its quota, of which 25 per cent must be paid in gold and the remainder in its currency.

Article III, Section 4(*a*), of the Articles of Agreement provides that a member must pay in gold 25 per cent of any increase in its quota, but that the Fund may reduce this percentage if a member's monetary reserves are less than its new quota on the date that it consents to a quota increase. The Executive Directors have never used this authority to reduce gold payments. However, in connection with the quota increases under the First and Second Resolutions adopted by the Board of Governors in February 1959[2] and all increases under the Compensatory Financing Decision of February 1963,[3] member countries were offered two alleviation facilities: they could increase their quotas by installments, or they could make special drawings up to an amount equal to their additional gold subscriptions.

The question whether the burden of gold payments should be alleviated was an important one during the Fourth Quinquennial Review of Quotas. The Executive Directors, after considerable discussion, again decided not to exercise the discretion given in Article III, Section 4(*a*), to reduce the impact of the required gold subscriptions. However, they decided on this occasion, as in 1959, that the facility of increases by installments should be available for increases under the First and Second Resolutions and that special drawings should be available to members in respect of increases under the First Resolution.

Where the installment facility is chosen, each installment of the quota increase will correspond to the amount of additional subscription in gold and currency paid by the member; the member must pay an original installment of its additional subscription, and an equal additional installment in each period of 12 months thereafter; each installment must be one fifth of the quota increase; and the member will have the right to accelerate its payments and quota increase under the original installment schedule.

Any country consenting to a quota increase under the First Resolution may request a drawing for an amount not exceeding 25 per cent of the quota increase. If the drawing is within the gold tranche, the established gold tranche policy and procedure will apply. If it is beyond the gold tranche, this special facility will be available to the member on the basis of its representation that it will encounter undue payments difficulties in making its gold subscription.

Repurchases corresponding to these exchange transactions beyond the gold tranche will normally be effected in equal annual installments to commence one year after the transaction, and to be completed not later than five years after the date of the transaction. However, if the member concerned represents that this schedule would create undue payments difficulties, the Fund may accept the member's representation that it will repurchase in accordance with the policies which apply to drawings from the Fund generally.[4]

Members' representations as to needs for drawings beyond the gold tranche or for a rescheduling of their repurchase commitments will not be challenged by the Fund except when it is clearly evident that they are without basis. The Fund will be prepared to grant waivers of the limits prescribed by Article V, Section 3(*a*)(iii),[5] in order to facilitate such exchange transactions.

Two arrangements were also made to mitigate the secondary impact of the additional gold subscriptions—i.e., the gold purchases which may be made from the members whose currencies are

[2] See *Annual Report, 1959,* pages 185-89.

[3] Executive Board Decision No. 1477-(63/8); see *Selected Decisions,* pages 40-43.

[4] Executive Board Decision No. 102-(52/11); see *Selected Decisions,* pages 21-24.

[5] Article V, Section 3(*a*)(iii), states that a member shall be entitled to buy the currency of another member from the Fund if the proposed purchase "would not cause the Fund's holdings of the purchasing member's currency to increase by more than twenty-five per cent of its quota during the period of twelve months ending on the date of the purchase nor to exceed two hundred per cent of its quota, but the twenty-five per cent limitation shall apply only to the extent that the Fund's holdings of the member's currency have been brought above seventy-five per cent of its quota if they had been below that amount."

reserve currencies by other members in connection with their subscriptions to the Fund.

First, a member which requests an exchange transaction as mentioned above is expected to consult the Managing Director on the currency to be drawn under Executive Board Decision No. 1371–(62/36) as mentioned below (p. 35). It is likely that many members which engage in such exchange transactions will use the currencies drawn to purchase gold from the monetary authorities of the countries whose currencies are drawn. They may wish to do this either to pay their additional gold subscriptions to the Fund or to restore the level of their gold holdings if they have already paid the additional subscriptions. Normally, such purchases of gold would be made from reserve currency members. With a view to alleviating the impact which such purchases would have on the gold holdings of the reserve currency members, the Fund will suggest that certain of these drawings, up to the equivalent of $150 million, be made in currencies which the Fund would then replenish by the sale of gold under Article VII, Section 2 (ii). In this way, the Fund's holdings of the currencies drawn would be replenished up to the amount of these purchases.

Second, in order to provide a further alleviation solely in connection with the quota increases under the two Resolutions, the Fund will make "general deposits" of gold totaling not more than the equivalent of $350 million with its depositories in the United States and the United Kingdom. Approximately $250 million will be placed on general deposit in the United States and $100 million in the United Kingdom. However, if the Fund determines that total sales of gold by these two countries in connection with the additional subscriptions of other members are less than the equivalent of $350 million, the Fund will reduce its general deposits accordingly. The amount of gold in the general deposits will be available to the Fund on demand for the use of or transfer to the Fund. A general deposit may be terminated or reduced at the request of the member in which the deposit is placed. On the occasion of any use of gold, the Fund would normally use, in appropriate proportions, earmarked gold and gold on general deposit in accordance with the good management of its assets.

Fund Transactions

Purchases and Stand-By Arrangements

During the past fiscal year, the Fund extended financial assistance to more members than in any previous year. Sales of currency exceeded all previous years with the exception of 1961-62, and the amount of stand-by arrangements agreed was almost identical with the record total reached in 1963-64. Purchases from the Fund were equivalent to $1,897.4 million (Table 49, p. 108) and the stand-by arrangements agreed during the year amounted to the equivalent of $2,159.1 million (Table 52, p. 109). Of the 34 members which received support from the Fund, either through direct purchase transactions or in the form of stand-by arrangements, 2 were industrial countries (the United Kingdom and the United States) and 32 were nonindustrial countries. The United Kingdom and the United States accounted for almost 78 per cent of total purchases and for more than 69 per cent of the total made available under stand-by arrangements. Of the members receiving financial assistance, 14 were in the Western Hemisphere, 7 in the Middle East, 6 in Africa, 4 in Asia, and 3 in Europe.

The largest purchase during the fiscal year was made by the United Kingdom early in December 1964; it comprised 11 currencies, totaling the equivalent of $1 billion, the full amount available under the stand-by arrangement. The Fund borrowed the equivalent of $405 million in the currencies of 8 members under the provisions of the General Arrangements to Borrow, and purchased 10 members' currencies with gold in amounts totaling the equivalent of $250 million (Tables 50 and 51, p. 108). The remainder of the U.K. drawing, equivalent to $345 million, was provided from the Fund's holdings of currencies. This was the first occasion on which the Fund made use of the General Arrangements to Borrow, which came into effect on October 24, 1962. In addition, Switzerland made available to the United Kingdom on a swap basis Sw F 345 million ($80 million) in accordance with the agreement between Switzerland and the Fund embodied in the exchange of letters of June 11, 1964.[6]

[6] Executive Board Decision No. 1712–(64/29); see *Annual Report, 1964,* pages 138-40, and *Selected Decisions,* pages 69-72.

Shortly after the close of the fiscal year, the United Kingdom drew a further $1,400 million from the Fund. In connection with this drawing, made in 11 currencies, the Fund purchased 10 members' currencies with gold for a total equivalent to $400 million, borrowed the equivalent of $525 million in 8 currencies under the provisions of the General Arrangements to Borrow, and provided the equivalent of $475 million from its own holdings (Tables 50 and 51). Switzerland made available Swiss francs equivalent to $40 million in accordance with its agreement with the Fund.

The currencies to be used when members make purchases from the Fund, or make repurchases other than under Article V, Section 7(*b*), are selected in accordance with the statement on Currencies to Be Drawn and to Be Used in Repurchases approved by the Executive Directors on July 20, 1962.[7] Fourteen currencies were supplied during the year to countries making purchases from the Fund, including, for the first time, Australian pounds and Mexican pesos. Eleven of these currencies were also used in repurchases, including for the first time Austrian schillings and Japanese yen. The currency most used, both for purchases and for repurchases, was the deutsche mark, of which $616.3 million was paid out and $283.9 million received in repurchases. Others used extensively for purchases included the French franc, the U.S. dollar, the Canadian dollar, and the Netherlands guilder. Details are given in Table 54, page 113. Details of repurchases under Article V, Section 7(*b*), are on page 114.

During 1964, the Fund's holdings of U.S. dollars continued to be above 75 per cent of the U.S. quota, which precluded the Fund from accepting U.S. dollars in repurchase from members, as explained in the 1964 Annual Report, page 11. The stand-by arrangement with the United States for $500 million, entered into in July 1963, expired in July 1964 with an unused balance equivalent to $250 million. In July 1964, the Fund entered into a new stand-by arrangement, also for the equivalent of $500 million. The first purchase by the United States, equivalent to $125 million, was made in February 1964; it was followed by further purchases equivalent to $125 million in June 1964, $150 million in September 1964, $125 million in December 1964, and $75 million in March 1965, totaling the equivalent of $600 million. The currencies purchased by the United States were intended for sale for U.S. dollars at par by the United States to those members of the Fund that keep their international reserves mainly in U.S. dollars and that had to make repurchases from the Fund. By April 30, 1965, 20 members had availed themselves of this facility, to a total of $543.2 million. However, dollars have continued to be purchased from the Fund by other members and this, together with other movements of U.S. dollars, had the effect of reducing the U.S. outstanding balance of drawings to $323 million on April 30, 1965. The U.K. drawing in May, referred to above, reduced this outstanding balance by another $200 million.

For members in need of financial assistance from the Fund, the stand-by arrangement has continued to be a valuable instrument. Five members, Burundi, Korea, Mali, Somalia, and Tunisia, entered into stand-by arrangements with the Fund for the first time. All except 9 of the purchases from the Fund during the past financial year were made under stand-by arrangements. Six of these 9 purchases—those by Cyprus, Iran, Israel, Morocco, Pakistan, and Panama—were within the gold tranche. Purchases by Cyprus, Morocco, and Panama constituted the first drawings by these members on the Fund's resources, although Morocco had in November 1959 entered into a stand-by arrangement for $25 million, which expired unused a year later.

In order to strengthen the confidence of members in the *de facto* automaticity of drawings in the gold tranche, the Executive Directors adopted a Decision on August 3, 1964[8] expediting the procedure for such drawings. This procedure makes it possible to deliver exchange to a member, when it is making a gold tranche drawing, two business days after receipt of the request by the Fund, thus reducing by three business days the normal period for effecting a drawing made under Article V, Section 3, of the Fund Agreement. By April 30, 1965, a total of 9 drawings had been consummated under this new procedure, including the last 4 drawings made by the United States.

[7] Executive Board Decision No. 1371–(62/36); see *Selected Decisions*, pages 33-39.

[8] See Appendix I, page 123.

With effect from June 1, 1964, the Board of Governors adopted an amendment of the terms and conditions prescribed in the membership resolutions of those members that had not yet agreed initial par values with the Fund. This Resolution authorized the Executive Directors to permit exchange transactions with a member prior to the establishment of an initial par value, under such conditions and in such amounts as might be prescribed by the Executive Directors. Similar terms will be incorporated in future membership resolutions.[9] By the end of April 1965, Korea and Mali had agreed with the Fund on provisional exchange rates for their currencies for this purpose and had entered into stand-by arrangements. Mali had drawn the equivalent of $9.9 million under its stand-by arrangement.

Technical Assistance

In response to requests from member countries, the Fund's technical assistance services were further expanded during the past year. The assistance given has been of two main types. The first has comprised the assignment of Fund officers for periods ranging from a few weeks to more than a year, to give advice on members' specific problems and programs. In some countries, these officers have assisted in the formulation of appropriate monetary, fiscal, and exchange policies, or in the implementation of stabilization programs. In others they have helped to draft legislation or to prepare monetary and balance of payments statistics. During the year 1964/65, staff officers were made available on long-term assignments to 10 members.

The second type of technical assistance has involved the engaging of experts from outside the staff to assist members in various specialized fields. These experts may serve as executive officers or as advisors. In accordance with this procedure, 6 experts from member countries have been recruited for senior positions in financial and economic institutions in the Democratic Republic of Congo, and others may be added. The two most senior of these experts have been serving as General Manager of the National Bank and Controller of Finance in the Ministry of Finance. This special Congo program is being carried out in close coordination with the United Nations.

Further progress has been made in the development of the two new branches of the Fund's work described in last year's Annual Report, the Central Banking Service and the Fiscal Affairs Department. The organization of the Central Banking Service was developed during the year to use the techniques of recruitment mentioned above. The Service was able to meet most of the 25 requests for technical assistance received from 18 countries. All those involving banking legislation and organization were handled by regular Fund staff members who went on advisory missions to the countries concerned, studied their problems, and made recommendations. Other requests were met by drawing on the Fund's pool of central banking experts from member countries; during the year, assignments were arranged, or negotiations for assignments completed, to provide 11 experts to fill positions ranging from advisory posts to the governorship of a central bank.

The establishment of the Fiscal Affairs Department in May 1964 has similarly enabled the Fund to respond more effectively to the requests of members for assistance in the fiscal field. Several officers of the Department have undertaken technical assistance assignments for short periods, and others have participated in regular staff missions visiting member countries where expertise in the fiscal field was required. In addition, two officers were recruited specially for long-term advisory assignments.

It became evident during the year that requests for long-term assistance, particularly in the fiscal field, would increase beyond the capacity of the Fund staff unless the number of persons available for assignment was substantially expanded. It was accordingly decided to establish an international panel of fiscal experts along the lines of the panel of central bank experts. These experts will be recruited from the more experienced fiscal agencies of member countries, several of which have already agreed to make personnel available. Those assigned may serve in either advisory or executive capacities, as budget experts, or tax administrators, or in similar posts in countries requesting assistance.

[9] Executive Board Decisions Nos. 1686–(64/22) and 1687–(64/22); see *Annual Report, 1964,* page 141.

The Fund may also recruit experts from time to time to meet specific requests for assistance in balance of payments or financial statistics.

The IMF Institute

The IMF Institute was established in May 1964 to expand and diversify the Fund's training activities.

One of the first tasks undertaken by the new Institute was to acquaint the French-speaking member countries which had recently joined the Fund with the general nature of the Fund, its policy objectives and financial resources, and the potential benefits of Fund training. For this purpose the Institute organized, between July and December 1964, two six-week seminars conducted in French for high officials from those countries. Each government in the French-speaking areas of Africa and one government in Asia was invited to designate a senior financial official to attend one of the seminars. Seventeen countries were able to take advantage of the invitation.

In March 1965, the Institute began the first of its regular 20-week courses on Financial Policy and Analysis conducted in English. Twenty participants, broadly representative of all areas of the world, attended this course. Of the 20 participants, 13 are employed in the Central Banks of their countries and 7 in Finance Ministries or Treasuries.

The emphasis of the course is on monetary and fiscal policy, with attention focused on, but not confined to, the problems of developing countries. It draws extensively on the experience that the Fund has gained in its contacts with member countries. The course has been formulated with the objective of enhancing the usefulness of the participants to their employing agencies. At the same time, it is hoped that the first-hand acquaintance which participants will gain with the Fund's objectives, operations, and procedures will contribute to a closer understanding and to smoother working relations between the Fund and its members.

In view of the nature of the regular course, participants have been selected with particular attention to their policy responsibilities. The Fund recognizes that governments in the developing countries may equally wish to send more junior staff members to Washington for studies which emphasize the technical aspects of financial and economic analysis. The IMF Institute is therefore planning to present over the years a variety of courses, dealing with subjects on different levels and addressed to officials of Central Banks, Ministries of Finance, and comparable government agencies in Fund member countries. The present professional staff of the IMF Institute consists of six economists, and it is intended to augment this number. During 1966, the Institute will move into new quarters where its technical accommodation will make it possible to handle several groups of participants at the same time.

The program for 1965-66 will comprise five different courses: (1) There will be two courses on Balance of Payments Methodology, one to be conducted in English from August 30, 1965 to October 8, 1965, and the other in French from February 21, 1966 to April 1, 1966; these two courses are designed to help member countries to improve their balance of payments statistics and their presentation for purposes of economic analysis. (2) Two courses will be given on Financial Policy and Analysis, the first to be conducted in French from October 14, 1965 to December 22, 1965 and the second in English from March 14, 1966 to July 29, 1966. (3) One Special Course, to be conducted in English from January 4, 1966 to February 11, 1966, will follow the general lines of the special courses given in French during July-August and October-December 1964.

* * *

Further particulars of Fund activities are given in a Supplementary Note, pages 107-19.

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Part II

REVIEW OF THE YEAR

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Chapter 5

Developments in the Industrial Countries

IN international financial relations, 1964 was marked by somewhat greater strains than had been experienced for some time. This was in contrast to the immediately preceding years, during which the structure of international payments had appeared on the whole to be improving. The strong pressures on the lira in March, and on sterling in November 1964—both of which were allayed by drawings on the Fund and by support from central banks and other financial institutions—were dramatic symptoms of these strains. Another was the activation of the General Arrangements to Borrow.

A general climate of prosperity continued to prevail in the industrial countries, but there were indications after mid-year that, while still strong, the expansionary forces in the world economy were not as powerful as they had been earlier. The very high rate of growth in world trade prevailing in 1963 and the early part of 1964 showed a tendency to moderate, as the rate of growth of imports of several industrial countries was slowing down. The measures taken by the United Kingdom to protect its balance of payments position, together with the less direct policies of restraint adopted by the United States, may accentuate this deceleration. Moreover, while the year witnessed an intensification of efforts in a number of countries to contain upward pressures on wages and prices, there was some relaxation toward the end of the year in the financial policies that several major countries had been following.

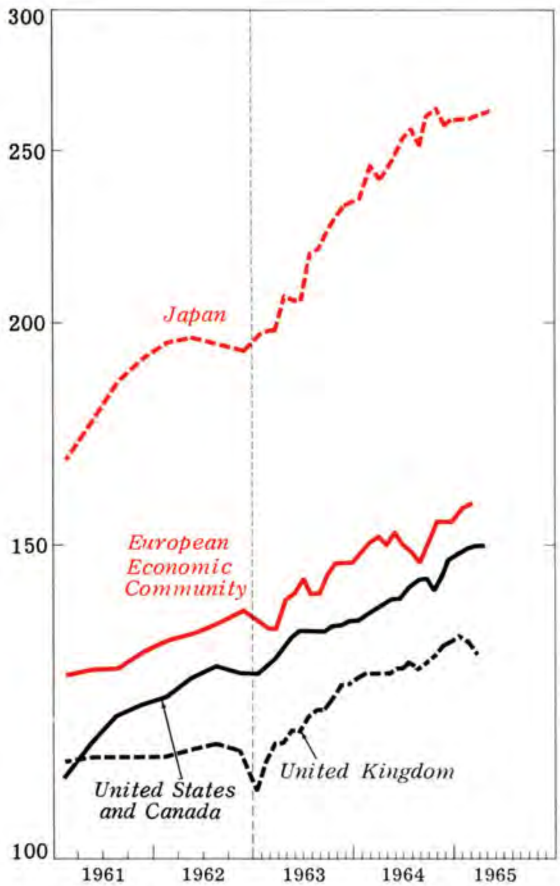
One significant corollary of the policies followed by individual countries to protect their balance of payments positions or to maintain domestic stability was a generally upward drift in the structure of interest rates. Some rates of international importance rose to levels which were quite high by the standards of the present century. Further, the narrowing of the spreads between rates in different countries, which seemed to be apparent early in the year, was replaced by a growing divergence in later months.

Production, Wages, and Prices

In most of the industrial countries, output continued to expand during 1964 at rates comparable to, even if somewhat less than, those prevailing in 1963 (Chart 3 and Table 6). In the United States, economic expansion continued for the fourth year in succession; but there was no further acceleration in the rate of advance. While unemployment declined, labor force time lost

CHART 3. SELECTED AREAS AND COUNTRIES: INDUSTRIAL PRODUCTION, SEASONALLY ADJUSTED, 1961–APRIL 1965

(1958 = 100)



through unemployment and part-time work stubbornly remained above 5 per cent. On the other hand, the rise in output in the United Kingdom was quite small until late in 1964, when there was a marked advance; unemployment continued to decline. In Japan, where the rise in output in 1963 had been greater than elsewhere, the rate

TABLE 6. GROSS NATIONAL PRODUCT AT CONSTANT PRICES: PERCENTAGE INCREASES FROM QUARTER TO QUARTER, 1962–FIRST QUARTER 1965

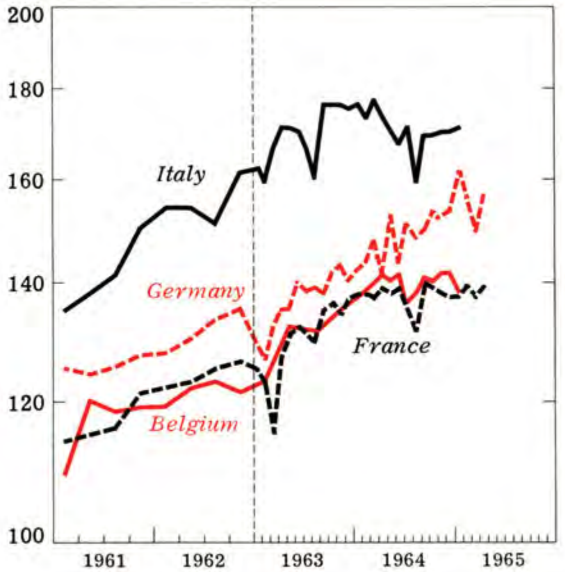
	Canada	Fed. Rep. of Germany[1]	Italy	United Kingdom[2]	United States
1962					
I	2.2	−5.9	1.8	−0.9	0.9
II	0.2	3.5	0.9	1.9	0.8
III	1.3	2.2	1.2	−0.3	0.3
IV	1.2	5.9	1.2	−0.3	1.2
1963					
I	1.2	−10.3	0.1	0.2	0.8
II	0.5	6.7	2.3	3.7	0.9
III	1.7	4.7	1.2	0.1	1.2
IV	2.2	5.5	1.1	3.9	1.4
1964					
I	2.4	−8.7	0.6	0.4	1.1
II	1.1	6.0	−0.5	0.5	1.0
III	0.5	2.6	−0.8	0.5	1.0
IV	0.9	7.3	1.2	2.2	0.6
1965					
I	2.7	...	...	...	1.7

[1] Not seasonally adjusted.
[2] Gross domestic product.

of advance decelerated during 1964 as a result of measures mainly directed toward protecting the balance of payments. For the European Economic Community as a whole, the index of industrial production has hardly risen since the first quarter of 1964, but there have been marked differences between individual countries (Chart 4). In the course of 1963, the main forces of expansion were operating in France and Italy. The excessive demand pressures in both these countries, which stimulated a rapid rise in domestic output but also appeared to threaten price stability, spilled over into Germany, where they contributed significantly to an acceleration of the rise in output. In Italy, where these developments had led to a major balance of payments deficit, measures were introduced progressively after May 1963 to restrain inflationary forces and to redress the balance of payments. These effectively restricted domestic demand and, in spite of a sharp rise in exports, brought about a slowdown in economic activity and a dramatic fall in imports. In France, measures to curb excessive domestic demand similarly resulted in a slowdown; industrial production

CHART 4. SELECTED COUNTRIES OF THE EUROPEAN ECONOMIC COMMUNITY: INDUSTRIAL PRODUCTION, SEASONALLY ADJUSTED, 1961–APRIL, 1965

(1958 = 100)



in that country fell in the third quarter of 1964 below the level reached in the last quarter of 1963. On the other hand, the upswing in Germany continued with increased vigor in 1964 and through the balance of payments helped, in turn, to moderate the slowdown in Italy and France. Where output continued to expand rapidly, domestic demand usually provided the main stimulus. Investment demand was particularly strong in Germany. Elsewhere, both investment and consumption have been exerting upward pressures.

The situation at the end of 1964 and early in 1965 was rather unclear, as shown by Table 7. A comparison of quarter-to-quarter changes in industrial production during this period is made difficult by the effect of strikes, the possibility of a major steel strike in the United States, and some statistical problems of measurement (e.g., the one apparent in the French series). The data in the table show that output in a number of industrial countries was continuing to rise; yet, with the exception of the United States, the increases in the fourth quarter of 1964 and the first quarter of 1965 were less than in the corresponding quarters of 1963 and 1964, respectively.

TABLE 7. INDUSTRIAL PRODUCTION: PERCENTAGE CHANGES FROM QUARTER TO QUARTER, 1962–FIRST QUARTER 1965

	Canada	France	Fed. Rep. of Germany	Italy	United Kingdom	United States
1962						
I	0.9	...	1.6	...	0.9	1.4
II	2.2	1.2	2.3	−3.4	0.9	1.5
III	1.4	1.4	1.5	0.2	0.9	1.0
IV	0.9	1.0	0.7	4.4	−0.9	0.2
1963						
I	1.0	−3.6	−3.0	1.3	−1.7	1.2
II	1.3	7.6	5.3	4.7	4.4	2.8
III	0.4	—	0.7	−1.7	1.7	1.1
IV	4.5	3.2	2.2	4.6	3.3	0.6
1964						
I	3.6	2.7	2.8	−0.5	1.9	1.5
II	0.3	0.4	0.7	−2.7	0.6	2.2
III	0.5	−3.7	2.0	−2.2	0.8	1.9
IV	2.5	3.3	2.0	1.8	1.6	0.8
1965						
I	2.9	−0.4	2.0	...	1.0	3.5

The general upward movement of wages persisted, particularly in continental Western Europe (Chart 5). Increases were especially rapid in the Netherlands, where the wage rate index for the fourth quarter of 1964 was 18 per cent above that for the comparable period in 1963. However, this overstates the increase in actual wage rates because in 1963 the so-called black wages, paid in addition to the rates set by collective bargaining, diminished. The wage agreement made late in 1964 envisaged a rise in wage rates of 5 per cent in 1965. Italy also experienced strong wage pressures, which, in combination with the slackening in the rate of advance, undoubtedly led to a marked increase in labor costs per unit of output; there are, however, signs that these pressures are now declining. Rising productivity, particularly in industry, appears to have offset the effect of rising wages on costs in Japan and Germany (Chart 6), but in Germany wages rose more than 7 per cent in the first half of 1965 over the first half of 1964, and this may endanger the stability of wage costs. In Canada and the United States, wage rates have continued to rise only slowly. Although some recent labor contract settlements in the United States have involved increases in hourly labor costs (including the effects of benefits other than higher wages) in excess of the "guideposts" outlined in the 1962 *Annual Report of the Council of Economic Advisers,* average labor costs per unit of output in manufacturing have thus far shown little change. In the United Kingdom, the authorities are concerned at the size of recent wage agreements although they realize that it will be some time before such agreements can be made consistent with government policy on incomes and prices as set out in a White Paper in April 1965.

These domestic pressures, together with some increase in import prices (Chart 7), contributed

CHART 5. SELECTED AREAS AND COUNTRIES: WAGE RATES, 1961–APRIL 1965

(1958 = 100)

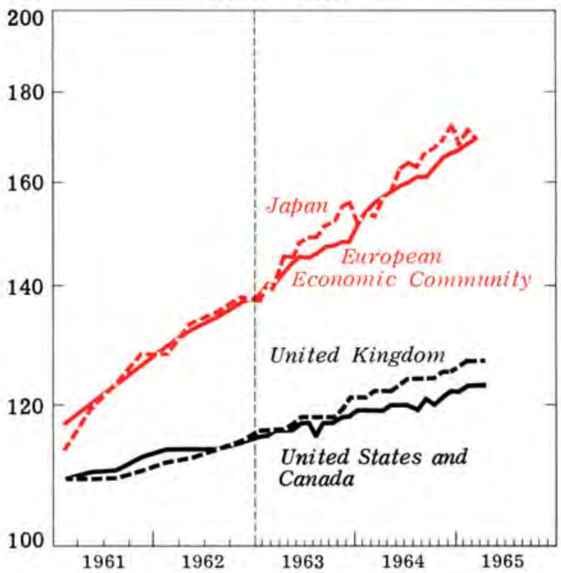
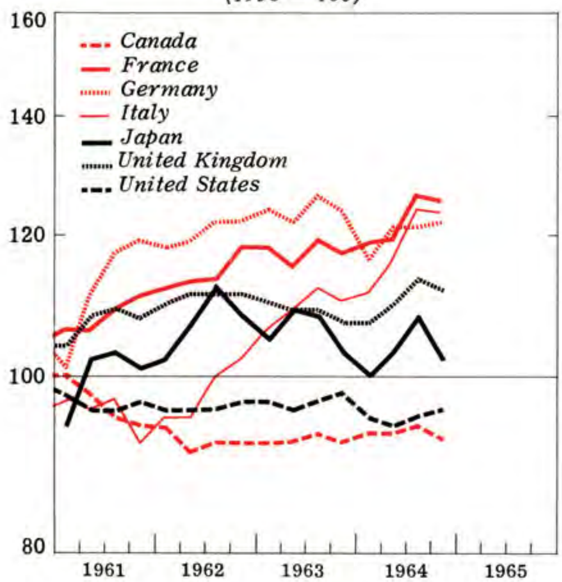


CHART 6. SELECTED COUNTRIES: WAGE COSTS PER UNIT OF OUTPUT IN MANUFACTURING, 1961-64

(1958 = 100)



in 1964 to a continuation of the upward movement of prices. Changes in wholesale prices largely reflect changes in wage costs (i.e., the effect of rising wage rates offset by rising productivity). For this reason, wholesale prices moved upward in Europe more slowly than wages, and they continued to be remarkably stable in the United States and Canada (Chart 8). Only in Japan (where wage costs in manufacturing have been tending to fall) was there evidence of a downward movement. Cost of living indices, which are more responsive to changes in wage rates, continued to rise somewhat more rapidly

CHART 7. SELECTED AREAS AND COUNTRIES: IMPORT PRICES, 1961–FIRST QUARTER 1965

(1958 = 100)

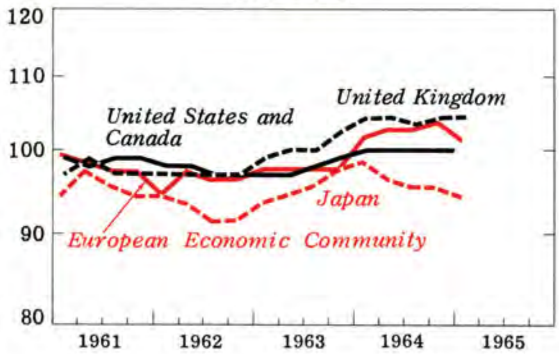
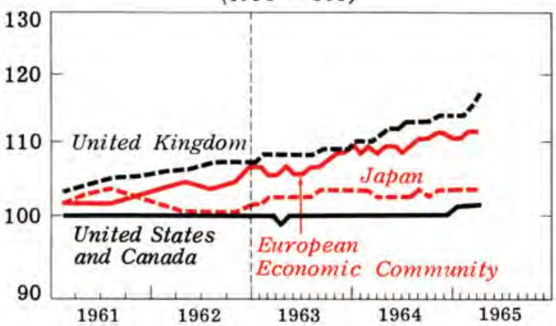


CHART 8. SELECTED AREAS AND COUNTRIES: WHOLESALE PRICES, 1961–APRIL 1965

(1958 = 100)



than wholesale prices (Chart 9). This increase was greatest in Italy and the Netherlands; rising money wages also contributed to a rather rapid increase in Japan. U.S. and Canadian export prices, on the whole, remained stable, but for the first time in several years there was a marked rise in the index for the EEC countries (Chart 10).

Incomes Policies

The fairly strong pressures on costs encountered in a number of countries in 1964 led to continued interest in the development of incomes policies, i.e., policies intended to ensure that the rate of increase of money income per capita should not outstrip the rise in average productivity per capita over the economy as a whole. The increasing integration of national economies makes it of growing importance that rises in domestic prices and costs, such as wages, remain in line with those in competing countries. At the

CHART 9. SELECTED AREAS AND COUNTRIES: COST OF LIVING, 1961–APRIL 1965

(1958 = 100)

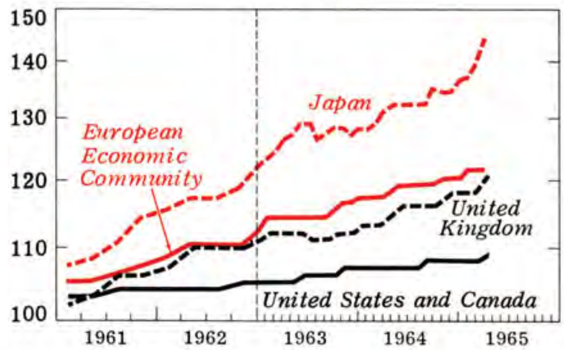
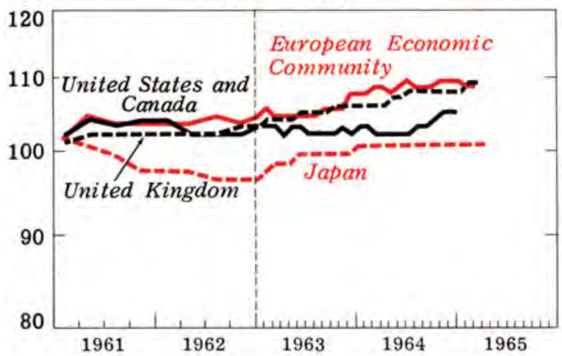


CHART 10. SELECTED AREAS AND COUNTRIES: EXPORT PRICES, 1961–APRIL 1965

(1958 = 100)



same time, wages and other costs cannot be kept below international levels, as is evidenced by the strong pressures in the Netherlands, which contributed to the recent marked increases in wages there. Furthermore, no incomes policy can be maintained unless accompanied by appropriate financial policies.

Progress during 1964 and the early part of 1965 toward the effective implementation of incomes policies was essentially limited to the development of institutional arrangements in the United Kingdom. These arrangements, which were set out in a White Paper published in February 1965, may be regarded as a prerequisite for further progress. Changes in wages and prices will be reviewed from time to time by the National Economic Development Council, assisted by government departments (which will in practice supply most of the necessary statistical data). The review of specific cases is to be the responsibility of a National Board for Prices and Incomes, comprising two divisions dealing, respectively with prices and with incomes. This Board, which was set up in April 1965, replaces the National Incomes Commission. The Government will retain direct responsibility for all cases referred to the Board, whether such referrals are made at the request of one or both parties involved, or of individuals, or on the initiative of the Government itself. The White Paper states that the Government will give the voluntary method every opportunity for success, but that it may resort to other methods if it becomes convinced that the voluntary method has failed. In particular, it will use its fiscal powers or other appropriate means to correct any excessive growth in aggregate profits, compared with the growth of the total of wages and salaries.

In a number of other countries, the vital task of persuading both sides of industry and other sectors of the economy of the need for an incomes policy has been undertaken. This, in itself, represents an important step toward the implementation of a policy. However, the specific policies to be followed have as yet been enunciated only in the most general terms. It is still too early to judge whether these developments will prove to be effective in countering cost inflation.

Financial and Other Policy Developments Before November 1964

Discount Rates

The most obvious sign of increasing financial restraint in some industrial countries is to be found in the rather general upward movement of central bank discount rates (Chart 11), the following changes being made prior to November:

	1964	Increase (Percentage points)	New Rate
Belgium	July 3	0.50	4.75
Denmark	June 11	1.00	6.50
Japan	Mar. 18	0.73	6.57
Netherlands	Jan. 6	0.50	4.00
	June 4	0.50	4.50
Sweden	Jan. 31	0.50	4.50
Switzerland	July 3	0.50	2.50
United Kingdom	Feb. 27	1.00	5.00

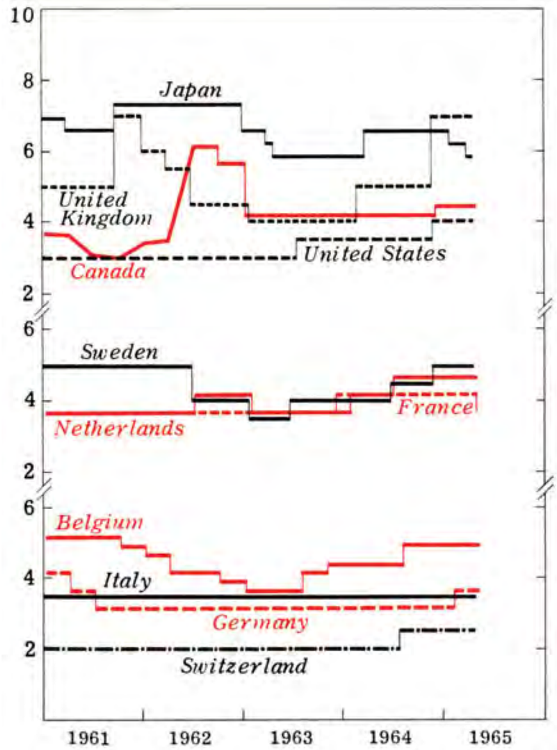
These increases, together with the maintenance of relatively low rates in Italy, Germany, and the United States, served to widen the spread between central bank rates which had been narrowing during 1963.

Monetary and Debt Management Policies

In many respects, the upward shifts in European discount rates and their stability in the

CHART 11. SELECTED COUNTRIES: CENTRAL BANK DISCOUNT RATES, 1961–APRIL 1965[1]

(In per cent per annum)

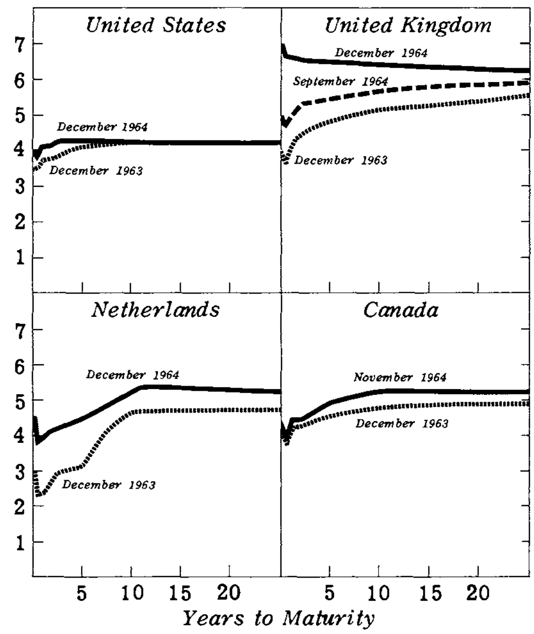


[1] Data for end of quarters, 1961-62; for end of months, 1963-65.

United States and Canada were symptoms of the somewhat disparate monetary, debt management, and fiscal policies followed during the year. These in turn reflected the disparate positions of the two areas. There was continued economic progress in the United States during the first part of 1964, leading to a rising demand for investment resources, but tax reductions and rising business and personal savings would probably have led to a decline in interest rates. This would have accentuated the undesirable balance of payments repercussions to which the rising interest rates and reduced credit availability abroad already tended to lead. Consequently, the authorities made policy adjustments that served to maintain a marked stability in the structure of rates (Chart 12). The free reserves of the commercial banks were kept relatively low, and debt management was directed to a lengthening of the average maturity of the government debt, so that the demand for securities by nonbank holders was satisfied, with very little change in bond prices.

CHART 12. TERM STRUCTURE OF INTEREST RATES

(In per cent)



In the United Kingdom, the authorities adopted policies in the early part of 1964 aimed at limiting the expansion of output to a rate which they believed could be sustained in the longer run. The increase in the bank rate from 4 per cent to 5 per cent in February 1964, and the policies of debt management pursued, served to raise the yields on government securities, particularly at the short end of the range. Monetary policy was intended to permit only a moderate increase in bank lending, but bank advances rose by 14 per cent in the 12 months ended in November. There were some declines in the banks' holdings of Treasury bills and British Government stocks.

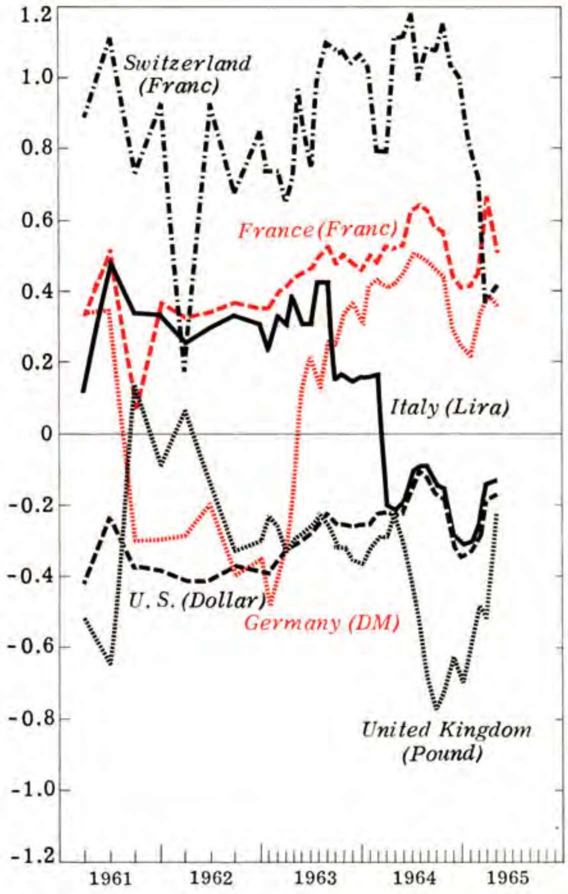
In Italy and Japan, pressures on the balance of payments had led to a tightening of monetary policies late in 1963 and early in 1964, as reviewed in last year's Annual Report. These policies were continued and in both countries contributed to a change from deficit to surplus in the current account and to a moderation of the pace of wage and price increases. In March, Italy made an additional swap agreement with the U.S. Treasury, arranged for credit facilities with other U.S. agencies and with European central banks, and some weeks later drew the equivalent of $225 million from the Fund. The facilities thus mobilized totaled approximately $1 billion. One important effect of the restrictive policies was a slowing down of the pace of industrial activity and a consequent relaxation of policies, starting in May.

Belgium, Denmark, Japan, the Netherlands, Sweden, and Switzerland increased their discount rates, and, with France and Germany, took other steps to restrict the liquidity of the commercial banks or to restrain the expansion of credit by them. On previous occasions, rising interest rates following restrictive changes in monetary policy have induced inflows of foreign funds which have served to augment the banks' liquidity and hence to offset the effects of monetary policy. For this reason, Denmark, Germany, Italy, Japan, and the Netherlands, among other countries, put limits on the increases of banks' foreign indebtedness or made provision for the neutralization of bank liquidity arising from this source. The Swiss National Bank established a new type of short-term security that it hoped would provide a basis for a domestic money market. Hitherto, the Swiss banks have held most of their liquid assets in the form of money-market balances in financial centers outside Switzerland, which has resulted in periodic movements of short-term funds occasioned by the banks' seasonal needs to obtain cash at the National Bank. It is hoped that the availability of this rather attractive new security will eliminate or reduce these movements.

Fiscal Policy

A number of countries also made use of fiscal policy as an instrument of general economic policy. In the United States, the most important fiscal change was the reduction in income and corporation taxes approved in February, which will result in reductions of $14 billion in tax liabilities in 1965. However, reductions in certain expenditures and the favorable effect of rising national income on government revenue and expenditure have served to limit the effect of reduced tax rates on the Government's cash deficit. In the United Kingdom, the fiscal outturn for the first half (April to September 1964) of the new financial year was considerably more favorable than had been expected from the estimates. Fiscal policy in Italy continued to be restrictive for a period after the pressures of monetary policy had been eased. In the Netherlands, the authorities tried to limit the growth of some categories of public expenditure by postponing investments and by imposing ceilings on long-term borrowing by local authorities who were already subject to ceilings on short-term borrowing. In Belgium, to counter inflationary pressures, the rising trend of government current expenditures was curtailed and some investment expenditures were postponed. There was a dramatic improvement in the budgetary situation in France. Expenditures rose at a slower rate than revenues, and revised estimates for the 1964 budget indicate an over-all deficit of F 850 million, compared with an original estimate of F 4,740 million. The 1965 estimates submitted by the Government envisaged a balanced budget for the first time in decades.

CHART 13. SELECTED COUNTRIES: EXCHANGE RATES, 1961–APRIL 1965[1]



[1] The premium or discount shown for each currency except the dollar is the difference between its premium or discount from par against the dollar and the average of the premiums or discounts against the dollar of the other members of the General Arrangements to Borrow and Switzerland. For the dollar, the discount is the inverse of the average of the premiums or discounts of the other ten currencies.

Subsequent Events

The Problems

From early in 1964, sterling was under intermittent pressure (Chart 13) and the United Kingdom had recourse to outstanding credit arrangements with the Federal Reserve Bank of New York, and to facilities arranged in September with the central banks of Belgium, Canada, France, the Federal Republic of Germany, Italy, the Netherlands, and Switzerland. In the fortnight of November 16-27, there was a large increase in the flow of international capital, particularly from the United Kingdom. This was associated with a loss of confidence and erratic movements in the international money markets. Not only did exchange rates move sharply, but wide spreads developed between comparable interest rates, even after allowance is made for the effects of forward cover (Charts 14 and 15). As the speculation continued, the central banks referred to above, together with those of Austria, Japan, and Sweden, the Bank for International Settlements, and the Export-Import Bank of Washington entered into arrangements with the United Kingdom, whereby the equivalent of $3 billion was made available to defend the parity of the pound. Early in December, the United Kingdom drew the full amount ($1 billion) of its outstanding stand-by arrangement with the Fund, using this, inter alia, to repay the credits arranged in September. These

CHART 14. COVERED SHORT-TERM INTEREST RATES, 1961–APRIL 1965

(In per cent)

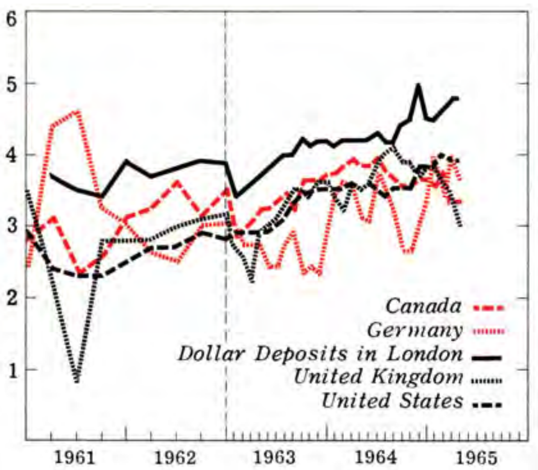
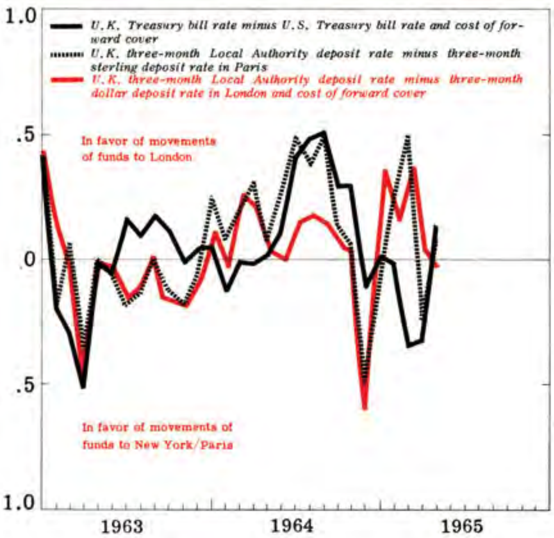


CHART 15. UNITED KINGDOM: TERM INTEREST DIFFERENTIALS, 1963–APRIL 1965

(In per cent per annum)



mainly short-term operations were designed to provide a breathing space during which more fundamental steps could be taken to correct the underlying disequilibrium. On February 10, it was announced that the November credits had been prolonged, and on May 25 the United Kingdom drew from the Fund the equivalent of $1,400 million, primarily to repay outstanding central bank credits. In connection with the two U.K. drawings, a total equivalent to $930 million was obtained by the Fund under the General Arrangements to Borrow, and the equivalent of $650 million by the sale of gold to members.

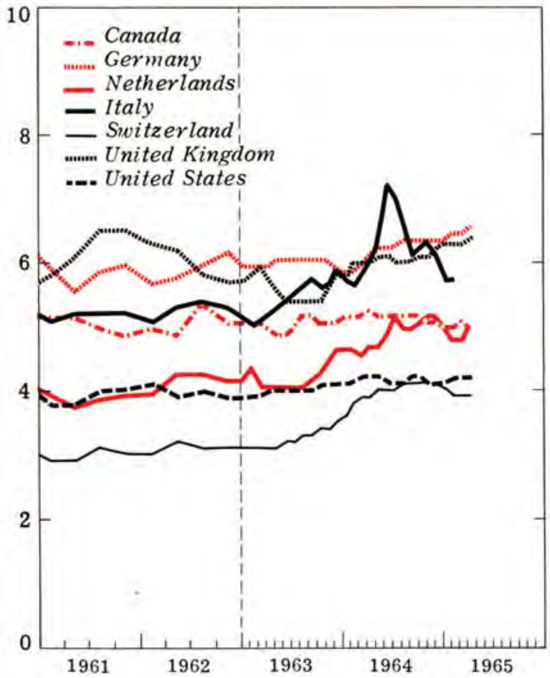
Changes in Policy

As early as October 25, the new U.K. Government had announced that it was taking steps to meet its balance of payments difficulties. On November 11, the Government introduced measures imposing a temporary charge of 15 per cent on most imports other than foodstuffs, unmanufactured tobacco, and basic raw materials, and providing for rebates of indirect taxes averaging 1.9 per cent of the value of exports. The surcharge was reduced to 10 per cent from April 27, 1965. A number of tax increases were also announced in November.

The announcement of these measures did not serve to prevent a further outflow of capital. Consequently, on November 23, the bank rate was raised from 5 per cent to 7 per cent; interest rates rose sharply and have remained high (Chart 16). To make the "credit squeeze" more effective, on December 8 the Governor of the Bank of England requested the banks and other financial institutions to limit advances for purposes other than exports and productive investment in manufacturing. Advances by the London clearing banks, seasonally adjusted, declined in January and February 1965 but turned upward again in March and April; on April 29, a call for special deposits by the domestic banks with the Bank of England was announced (for the London clearing banks the amount called was equivalent to 1 per cent of deposits). The Governor of the Bank of England asked the banks to limit the expansion of credit to 5 per cent in the 12 months to March

CHART 16. SELECTED COUNTRIES: LONG-TERM GOVERNMENT BOND YIELDS, 1961–APRIL 1965

(In per cent per annum)



1966; he also requested a comparable degree of restraint from other financial institutions. The budget statement of April 6 outlined the Government's plans for restoring a balance in external payments by the second half of 1966. Its two key points were that, by the early months of 1966, the Government intended to reduce the pressure on resources by £250 million at an annual rate, and to reduce, by changes in the exchange controls, the outflow of long-term capital by at least £100 million at an annual rate. On June 3, the bank rate was lowered to 6 per cent, but the other elements of financial restraint remained in force, and hire-purchase regulations were tightened.

The deterioration of the structure of international payments during November 1964 induced a further general rise in interest rates. Immediately after the increase in the Bank of England discount rate, the discount rates of the Federal Reserve Banks in the United States were raised from 3.5 per cent to 4.0 per cent, and the ceilings on interest rates payable on savings and time deposits with commercial banks in that country were raised. These steps were taken to offset the attractiveness of foreign short-term rates for internationally volatile funds. The Bank of Canada responded to the rise on November 23 in the U.K. bank rate and the Federal Reserve discount rate by increasing its bank rate from 4.0 per cent to 4.25 per cent later the same day. The Sveriges Riksbank's rate had been raised from 4.5 per cent to 5.0 per cent on November 6. These various measures served to push some rates, particularly the Euro-dollar rate, to markedly higher levels. Throughout the early part of 1965, the Federal Reserve maintained rather tight bank liquidity positions. During this period, also, the U.S. Government proposed a two-year extension of the Interest Equalization Tax, its broadening to cover bank credit with maturities of one to three years, and its extension to cover nonbank credit. The Government also appealed for a program of voluntary restraint on international lending operations by U.S. financial institutions and other businesses. On January 22, the Bundesbank raised its discount rate from 3 per cent to 3.5 per cent in order to counteract persistent excessive demand and the danger of price increases. As a consequence, the high cost of domestic short-term finance prevailing at the end of 1964 was pushed even higher.

France, Italy, and Japan were the most important countries to show signs of moving against this tide. From October, public sector investment in Italy has been increased, in order to encourage a renewal of economic growth, and interest rates have been declining. The Japanese authorities, faced with an improved balance of payments position based on rising exports, turned to more expansionary policies in order to impart a new impetus to economic expansion. The reserve requirements for bank deposits other than time deposits were cut in half, returning them to their level in December 1963. The Bank of Japan's discount rate was lowered on January 9 from 6.57 per cent to 6.205 per cent, and on April 3 to 5.84 per cent. On April 8, the Bank of France's discount rate was reduced to 3.5 per cent. It is possible that these changes may indicate that the general levels of international interest rates have passed their peaks. In February and March, rates in several countries were lower than they had been in the immediately preceding months.

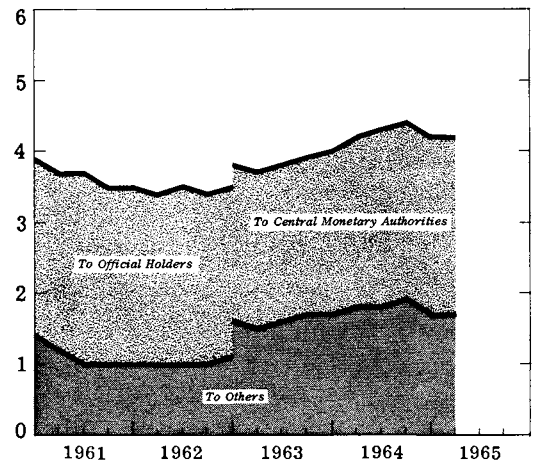
Foreign Exchange Markets

Whereas 1963 could be described as a year of relative calm in the international exchange markets, 1964 and the early part of 1965 covered a period of fairly severe stress. In March, the lira was under heavy pressure. In the second half of the year, sterling was generally weak; and after a temporary recovery early in 1965 it suffered a second setback, which was not overcome until after the budget statement in April. Early in 1965 the dollar also weakened, but this tendency was reversed by the announcement of the new balance of payments program. Together, these movements provide the main explanation for the apparently rather erratic changes in the quotations for other currencies, which tended to be the inverse of those of the two reserve currencies. Sharp movements in rates in November provided the most dramatic events in the markets in 1964.

In part, these movements in exchange rates were associated with rather considerable changes in foreign nonofficial sterling holdings (Chart 17) and dollar balances (Chart 18). It is possible that the high interest rates prevailing in the Euro-dollar market may well serve to make these tendencies persist by acting as an attraction for the transfer of foreign bank and other nonresident balances from the United States to Europe while remaining denominated in dollars.

CHART 17. U.K. EXTERNAL STERLING LIABILITIES, 1961–MARCH 1965

(In billions of pounds sterling)



Development of Securities Markets

Last year's Annual Report drew attention to the desirability of improving the structure of securities markets in Europe, partly to make easier the role of capital movements in facilitating balance of payments adjustment. There has been little integration of the individual European capital markets, although the problem is being intensively studied.

As indicated in Table 8, the total issues of new securities on markets other than those of the borrowing country were slightly higher in 1964 than in 1963; and in the early part of 1965 these offerings for other borrowers continued at close to their 1964 levels. The increase in 1964 was the product of substantial offerings in the United States and Germany, and increases in other important markets (see Table 9), of which London (where total new offerings of sterling and foreign currency securities rose from the equivalent of $280 million to $583 million) and Germany were the most important. The international market has been dominated by Canadian and European issues, although Japan, Australia (in 1963), and some European countries have also been important participants, as indicated in Table 10.

Tables 8 and 9 illustrate an important development during 1964: the increase in issues in currencies other than those of the markets where

CHART 18. U.S. INTERNATIONAL LIQUID LIABILITIES, 1961–MARCH 1965

(In billions of U.S. dollars)

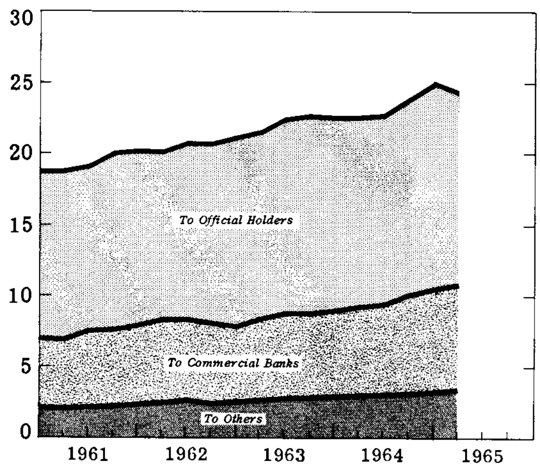


TABLE 8. ISSUES OF SECURITIES ON MARKETS IN COUNTRIES OTHER THAN THAT OF BORROWER

(In millions of U.S. dollars)

	Issues in Currencies Other than That of Country Where Issued						
	In London[1]	In Luxembourg	In New York	Total	Issues in Units of Account[2]	Issues in Currency of Country Where Issued	Total Issues
1963	89	32	—	121	48	1,849	2,018
1964	442	17	40	499	10	1,650	2,159
1965							
I	87	—	25	112	—	546	658

[1] Including issues denominated in external sterling and issues made optionally in London or Luxembourg. Excluding two issues made optionally in deutsche mark.
[2] All issued in Luxembourg.

TABLE 10. AMOUNTS RAISED BY ISSUES OF SECURITIES ON MARKETS IN COUNTRIES OTHER THAN THAT OF BORROWER, 1963–MARCH 1965

(In millions of U.S. dollars)

	1963	1964	1965 Jan.-Mar.
International institutions	47	178	262
Europe	626[1]	699	175
European institutions	*40*	*145*	*37*
Denmark	*85*	*136*	—
Finland	*18*	*108*	*21*
Norway	*77*	*120*	*69*
Canada	789	725	100
Japan	246	213	25
Australia	120	—	25
Other sterling area	89	95	31
Other	102	250	40
Total	2,018	2,159	658

[1] Including $115 million for Shell Funding Corporation in New York.

issued, referred to as foreign currency issues. These included all those made in Luxembourg, a large proportion of those in London, and a small proportion of those in New York.

The effects of the U.S. Interest Equalization Tax, from the date (August 1963) of its impact on the New York market (the most important international center for the issue of long-term securities) were quite important. While the total value of foreign new issues in the United States was somewhat less in 1964 than in 1963, the main effect of the Tax, as indicated in Table 11, was to reduce the issues by borrowers from European countries (except Finland, to which the Tax does not apply) and Japan, but to make the New York market relatively more favorable for borrowers from the developing countries. It is to be expected that the program of voluntary balance of payments restraint announced in February 1965 will intensify this tendency, even though the height of European interest rates (e.g., the Euro-dollar rates) might encourage European borrowers to raise funds on the New York market. In 1964, the decline in foreign issues was more than offset by an increase in bank loans to borrowers who might otherwise have floated long-term bonds, but in February 1965 the Tax was also applied to bank loans for one year or more.

In March 1964, Germany announced its intention of altering its tax policies, to bring them more into line with general practices, by imposing a 25 per cent withholding tax on remittances of interest to foreign holders of German fixed-interest securities. This had the prospective effect of reducing substantially the net yield on German securities held by foreigners who were unable to obtain relief under double taxation agreements. The announcement led to a sharp fall in the foreign demand for German securities. The tax took effect

TABLE 9. FOREIGN ISSUES OF SECURITIES IN CURRENCY OF MARKET WHERE ISSUED

(In millions of U.S. dollars)

	United States	United Kingdom[1]	France	Fed. Rep. of Germany	Italy	Netherlands	Switzerland	Total
1963	1,443[2]	191	12	40	24	3	136	1,849
1964	1,155	141	30	224	—	15	84	1,650
1965								
I	360	31	—	146[3]	—	—	9	546

[1] Fund estimate.
[2] Including Shell Funding Corporation, $115 million.
[3] See footnote 1 to Table 8.

TABLE 11. SALES OF NEW ISSUES BY FOREIGN BORROWERS IN THE UNITED STATES[1]

(In millions of U.S. dollars)

	Europe	Canada	Other Western Hemisphere	Japan	Other Asia and Africa	Other	Total
1963							
I	65	348	13	42	18	—	486
II	154	260	—	65	17	17	513
III	19	61	23	52	11	20	186
IV	34	24	—	5	22	—	85
1964							
I	—	86	13	—	25	4	127
II	11	187	56	—	30	—	284
III	—	44	14	—	13	—	71
IV	24	383	125	—	49	—	581
1965							
I	9	99	5	—	29	160	302

Source: U.S. Department of Commerce, *Survey of Current Business.*

[1] Purchases by U.S. residents, i.e., excluding purchases by non-U.S. residents of foreign issues in New York, included in Tables 9 and 10.

from July 1, 1965. It does not, however, apply to the income from foreign securities issued in the German market (a large proportion of which are normally purchased by foreign investors); this should assist in the development of an international capital market there. Meanwhile, early in May, the persistence of strong demand for capital pushed the yield on government bonds to 7 per cent.

A second important change in the German securities market was the abolition, with effect from January 1, 1965, of the 2.5 per cent tax on all new issues; while the major part of German bond issues were already exempt from the tax, issues on behalf of industry and foreigners were not. The removal of the tax will, therefore, tend slightly to offset the high cost of borrowing in German markets. In fact, foreign issues in the German bond market increased from the equivalent of $45 million in the first four months of 1964 to $146 million in the first four months of 1965, of which the largest share was sold to nonresidents.

In addition to the foregoing changes in the international securities markets, a number of changes have been introduced in national markets with the intention of making those markets more accessible for purely domestic issues. Attempts are being made—e.g., in France, Germany, and Italy—to improve the operation of the local securities markets so as to stimulate investor interest and attract funds. In Italy, insurance companies are now permitted to invest a proportion of their reserves in long-term private securities, and a law has been passed permitting the establishment of investment trusts. These steps, taken to widen the base of investment in the market, may lead to greater stability of security prices. In France, the tax on income from dividends was modified to increase the effective yield of shares. There was also an easing of the tax on capital gains. In the United Kingdom, the imposition of such a tax may work in the opposite direction, although the existence in the United States of a tax on capital gains has not deterred the growth of securities markets. The reform of company law in Germany should strengthen the position of shareholders and thereby increase interest in the acquisition of shares. A new law in Italy, granting tax benefits to companies planning to merge, is likely to lead to a series of amalgamations and an increase in the average size of companies. A projected change in the law governing companies in France would also facilitate company mergers. And, of course, larger companies tend to rely rather more heavily on the new issue market than is typical of smaller companies. These developments will add to the importance of the measures described above to strengthen the domestic securities markets in some of the leading European countries.

Chapter 6

World Trade, Payments, and Reserves

World Trade

THE exceptionally high rate of expansion in almost all the industrial countries during 1963 and the continued prosperity in most of them in 1964 were associated with a rapid growth in world trade. The value of world exports, excluding those of Soviet countries and Mainland China, rose by no less than 12 per cent from 1963 to 1964, following an increase of 8½ per cent from 1962 to 1963 and one of nearly 5½ per cent from 1961 to 1962. The accelerated rate of growth from 1963 to 1964 was due in part to a faster rise in export prices (Table 12). These prices were higher than in 1963 in all the manufacturing countries except Japan, and in most primary producing countries, other than those exporting petroleum. The volume of world trade was about 10 per cent greater in 1964 than in 1963, compared with an increase of about 7½ per cent from 1962 to 1963.

TABLE 12. EXPORT UNIT VALUES, 1961-64

(1960 = 100)

	1961	1962	1963	1964	1964 Fourth Quarter
Manufacturing countries					
United States	102	102	101	102	104
EEC countries[1]	102	102	102	104	106
EFTA countries[2]	100	101	102	105	106
Japan	95	92	95	93	92
Primary producing countries					
Canada	101	104	105	106	107
Australia, New Zealand, South Africa	99	100	107	112	110
Other primary producing countries outside Europe	97	95	97	99	98
Of which					
Petroleum producing countries	97	98	97	97	97
Other	97	94	97	100	99

Sources: International Monetary Fund, *International Financial Statistics;* United Nations, *Monthly Bulletin of Statistics,* April 1965.

[1] Belgium-Luxembourg, France, Federal Republic of Germany, Italy, Netherlands.

[2] Austria, Denmark, Norway, Sweden, Switzerland, United Kingdom.

Changes in Trade, 1963-64

The value of trade between manufacturing countries increased by about 13½ per cent, which was again somewhat greater than the rise in world trade generally, or in the total exports or imports of the manufacturing countries to or from all sources. However, manufacturing countries' exports to primary producing countries in Europe and the higher income primary producing countries outside Europe (Group I in Tables 13 and 14) increased by an even greater percentage, as did the exports of both this group of primary producing countries and the manufacturing countries to the Sino-Soviet Area. The latter increase was in part attributable to very large rises in agricultural exports to the Soviet Union from the United States, Canada, and Australia, and a sharp increase in Japan's exports of manufactures to Mainland China. The value of trade between the

TABLE 13. DIRECTION OF WORLD TRADE, 1963 AND 1964

(In billions of U.S. dollars)

Exports from	Year	Exports to: Manufacturing Countries	Primary Producing Countries: I[1]	Primary Producing Countries: II[2]	Sino-Soviet Area[3]	World
Manufacturing countries[4]	1963	49.3	13.7	21.5	2.6	87.1
	1964	55.9	15.8	23.5	3.1	98.3
Primary producing countries						
Group I[1]	1963	11.8	0.9	2.1	1.2	16.0
	1964	13.4	1.1	2.2	1.7	18.4
Group II[2]	1963	20.6	2.4	6.6	1.4	31.0
	1964[5]	22.4	2.6	7.1	1.6	33.7
World, excl. Sino-Soviet Area[4]	1963	81.7	17.0	30.2	5.2	134.1
	1964[5]	91.7	19.5	32.8	6.4	150.4
Sino-Soviet Area[3]	1963	3.2	0.9	2.1	12.6	18.8
	1964[5]	3.5	...	...	...	...

Sources: International Monetary Fund and International Bank for Reconstruction and Development, *Direction of Trade;* International Monetary Fund, *International Financial Statistics,* and staff estimates.

[1] Australia, Canada, New Zealand, South Africa, and primary producing countries in Europe.

[2] All other primary producing countries.

[3] Including Cuba.

[4] Military exports from United States are excluded.

[5] Preliminary estimates.

manufacturing countries and the less developed countries (Group II) rose less than world trade in general, expanding by some 9 per cent in each direction.

The very slight growth of U.K. trade was in striking contrast to this general expansion. The value of U.K. imports (which account for more than one sixth of all manufacturing countries' imports from the less developed countries) increased by only about 1½ per cent, and U.K. exports to the group showed no increase at all. U.S. imports from them also rose comparatively little (by about 5½ per cent, compared with an increase of over 11½ per cent in imports of EEC countries), but U.S. exports to the group rose faster than the average. Japan's trade in each direction rose in value by nearly 16 per cent.

By contrast, the United Kingdom's imports from manufacturing countries rose much more than the average. Table 15 (which details the corresponding export flows) shows that U.K. purchases from manufacturing countries rose by about 19½ per cent, while those of other EFTA countries, the EEC as a group, the United States, and Japan each rose by about 12½-13½ per cent. Japan, Italy, Norway, the United States, and the Federal Republic of Germany all increased their exports to the United Kingdom by 20-25 per cent or more.

The United Kingdom's exports to manufacturing countries rose by only 5 per cent—i.e., little over one third as fast as those of the other manufacturing countries. U.K. exports to other EFTA countries rose no faster than those of EEC countries, and slightly less than those of the United States; its exports to the United States rose less than half as fast as those of other manufacturing countries, and there was scarcely any increase in the value of its exports to the EEC countries. U.S. exports (excluding special categories) to these countries, however, rose almost as fast as their exports to each other.

TABLE 14. GROWTH IN VALUE OF TRADE BETWEEN MAJOR AREAS, 1961-64

(Percentage increase over preceding year)

Exports from	Year	Exports to: Manufacturing Countries	Primary Producing Countries: I[1]	Primary Producing Countries: II[2]	Sino-Soviet Area[3]	World
Manufacturing countries[4]	1961	8.9	1.5	5.0	0.3[5]	6.0
	1962	9.6	3.5	−1.4	7.5	5.6
	1963	10.5	10.1	4.5	2.0	8.6
	1964	13.4	15.3	9.3	19.2	12.9
Primary producing countries						
Group I[1]	1961	5.1	5.4	2.1	47.0	6.9
	1962	3.5	5.6	−5.7	−1.0	2.4
	1963	5.4	12.0	12.4	50.0	9.9
	1964[6]	13.6	22.2	4.8	41.7	15.0
Group II[2]	1961	1.0	−2.2	...	...	1.0
	1962	5.5	22.0	5.9	−2.3	5.8
	1963	7.0	8.0	8.0	8.0	7.3
	1964[6]	9.0	8.0	8.0	14.0	8.7
World, excl. Sino-Soviet Area[4]	1961	6.1	2.1	3.6	—	4.7
	1962	7.6	5.5	—	4.4	5.4
	1963	8.8	10.4	6.3	10.6	8.5
	1964[6]	12.2	14.7	8.6	23.1	12.2
Sino-Soviet Area[3]	1961	1.4[5]	−6.4	8.4	5.6	2.3
	1962	12.6	36.7	24.7	4.9	9.1
	1963	9.0	13.5	11.0	5.5	7.0
	1964[6]	9.0	...	...	...	...

Sources: See Table 13.

[1] Australia, Canada, New Zealand, South Africa, and primary producing countries in Europe.
[2] All other primary producing countries.
[3] Including Cuba.
[4] Military exports from United States are excluded.
[5] Excluding large changes in Cuba's trade over this period.
[6] Preliminary estimates.

Trade in Manufactures

Much of the deterioration in the United Kingdom's trading position seems to have been associated with the exceptionally high level of domestic investment during 1964. Pressure on the capacity of the engineering sector was apparently one reason why imports of machinery and transport equipment rose by more than one third in value from 1963 to 1964, while exports of these goods showed practically no change (Table 16). There were, however, some more specific reasons for the slow growth of such exports, namely, fewer deliveries of ships, aircraft, and aircraft engines, sales of which frequently vary sharply from one year to another, a fall in exports to the U.S.S.R., and the weakness of the Italian automobile market. The value of U.K. exports of other manufactures rose by some 10 per cent, compared with a 13 per cent increase in the value of all imports other than machinery and transport equipment. There was, however, virtually no increase in the value of U.K. exports of foodstuffs, materials, and fuels, owing to a marked decline in exports of mineral fuels.

The striking difference between the two broad classes of manufactures is also evident in the comparison between the growth of U.K. exports and imports and of those of other countries in trade

Table 15. Trade Between Manufacturing Countries, 1963 and 1964

Exports from	Year	Exports to: United Kingdom	Other EFTA Countries	EEC Countries	United States	Japan	All Manufacturing Countries[1, 2]
		Value in millions of U.S. dollars					
United Kingdom	1963	—	1,360	2,500	1,020	140	5,020
	1964	—	1,490	2,540	1,070	160	5,270
Other EFTA countries	1963	1,280	1,700	3,530	720	90	7,330
	1964	1,530	2,020	3,830	800	130	8,310
EEC countries	1963	1,980	5,720	15,790	2,560	360	26,400
	1964	2,280	6,290	18,390	2,860	390	30,200
United States[2]	1963	1,170	860	3,970	—	1,710	8,380
	1964	1,470	960	4,560	—	1,910	9,460
Japan	1963	160	120	330	1,520	—	2,130
	1964	200	200	370	1,870	—	2,630
All manufacturing countries[1, 2]	1963	4,590	9,750	26,110	5,820	2,300	49,260
	1964	5,480	10,970	29,690	6,590	2,590	55,870
		Percentage increases, 1963 to 1964[3]					
United Kingdom		—	10.1	1.6	5.2	14.0	5.0
Other EFTA countries		19.6	18.8	8.5	11.0	36.2	13.4
EEC countries		15.1	9.9	16.4	11.5	9.5	14.4
United States[2]		25.4	12.5	15.0	—	11.8	12.9
Japan		26.9	73.0	10.2	22.6	—	23.5
All manufacturing countries[2]		19.4	12.5	13.7	13.2	12.6	13.4

Source: International Monetary Fund and International Bank for Reconstruction and Development, *Direction of Trade*.
[1] Because of rounding, the figures shown may not add to totals.
[2] Excluding military exports. Figures in last column include estimate of U.S. special category exports, which cannot be allocated between the areas shown in the table.
[3] Calculated from unrounded figures.

with particular areas presented in Table 17. Table 18 indicates the relative importance of the two groups of manufactures in the imports and exports of the United Kingdom, other EFTA countries, EEC countries, the United States, and Japan.

Table 16. United Kingdom: Value and Growth of Trade in Three Major Categories, 1964

Commodity Grouping	Value in 1964: Exports	Value in 1964: Imports	Increase over 1963: Exports	Increase over 1963: Imports
	Million U.S. dollars		*Percentage*	
Machinery and transport equipment[1]	5,113	1,526	1	34
Other manufactures[2]	4,790	4,105	10 } 7	26 } 13
All other goods[3]	2,008	9,806	1	8

Source: United Kingdom Report on Overseas Trade, February 1965.
[1] Standard International Trade Classification (SITC) Group 7.
[2] SITC Groups 5, 6, and 8.
[3] SITC Groups 1-4 and 9.

Table 17 (which relates to the first nine months of each year) shows the United Kingdom's exports of manufactures other than machinery and vehicles to the rest of Western Europe did almost as well as those of the United States and of other EFTA countries; exports from the EEC countries rose one-third faster. U.K. exports of these goods to the United States and Canada also increased almost as fast as those of the EEC countries. But British exports of machinery and transport equipment to Western Europe showed only a slight increase, compared with increases of 9 per cent in exports both from the United States and from the other EFTA countries, and of 15 per cent in exports from EEC countries; U.K. exports of such manufactures to the United States and Canada rose only half as fast as those of the EEC countries. As a consequence, the United Kingdom's share in the imports of machinery and vehicles into both the EEC countries and the United States dropped sharply be-

TABLE 17. GROWTH OF MANUFACTURING COUNTRIES' TRADE IN MACHINERY AND TRANSPORT EQUIPMENT AND OTHER MANUFACTURES, BY AREAS[1]

(Percentage increases from Jan.-Sept. 1963 to Jan.-Sept. 1964)

	Trade of				
Commodity Grouping and Direction of Trade	United Kingdom	EEC Countries	United States[2]	Other EFTA Countries[3]	Japan[4]
Imports of countries shown in column head from areas listed below					
Of machinery and transport equipment from					
United Kingdom	—	2	0	10	12
Other Western Europe	35	13	11	11	
United States and Canada	40	15	13[5]	16	—13
World	35	12	12	13	—4
Of other manufactures from					
United Kingdom	—	14	7	20	43
Other Western Europe	28	20	12	16	
United States and Canada	41	8	5[5]	23	48
World	29	18	10	19	50
Exports of countries shown in column head to areas listed below					
Of machinery and transport equipment to					
United Kingdom	—	14	44	45	70
Other Western Europe	2	15	9	9	
United States and Canada	9	19	23[5]	12	31
Australia, New Zealand, and South Africa	7	19	67[6]	76	...
Less developed countries	—2	9	14[7]	...	...
World	2	14	18	13[8]	24
Of other manufactures to					
United Kingdom	—	23	51	32	7
Other Western Europe	15	20	16	16	
United States and Canada	8	10	17[5]	16	27
Australia, New Zealand, and South Africa	10	22	22[6]	11	...
Less developed countries	4	9	14[7]	10	...
World	10	16	16	17	15

Sources: United Nations, *Economic Survey for Europe, 1964;* Statistical Office of the EEC, *Monthly Foreign Trade Statistics;* U.S. Department of Commerce, *U.S. Overseas Business Reports* and *United States Trade with Major World Areas, January-September 1964* (December 1964); United Nations, Commodity Trade Statistics; and Japanese Ministry of Finance, Customs Statistics.

[1] Commodity groupings as in Table 16.
[2] Change in exports, excluding special categories.
[3] Including Finland.
[4] Percentage changes partly estimated.
[5] Trade with Canada only.
[6] Australia and New Zealand.
[7] Also includes South Africa.
[8] Excluding trade with Eastern Europe, which declined by one third.

tween the two periods, whereas its share in their imports of other manufactures was much more nearly maintained. Table 17 also illustrates the relatively favorable development of U.K. trade with the EFTA countries. The United Kingdom's share in their imports of manufactures other than machinery and vehicles actually increased slightly, and there was only a slight reduction in its share of their imports of machinery and vehicles.

Table 17 also throws some interesting light on the comparative development of exports of manufactures from the United States and the EEC countries. It shows that, owing to a greater rise in the value of its exports of machinery and transport equipment, U.S. exports of manufactures rose proportionately somewhat more that those of the EEC countries between January-September 1963 and January-September 1964. This was due, however, in large measure to an increase of nearly 50 per cent in U.S. exports of manufactures to the United Kingdom, and to an even greater percentage increase in its exports of machinery and vehicles to Australia and New Zealand. U.S. exports of both groups of manufactures to the less developed countries also rose faster than the comparatively small exports of EEC countries to this area, while U.S. exports to continental Western Europe as a whole rose considerably less than those of EEC countries. However, EEC countries' imports of manufactures from the United States rose at about the same rate as their imports from each other (see Table 19).

The faster than average expansion in the manufactured exports of the United States and Japan

TABLE 18. VALUE OF MANUFACTURING COUNTRIES' TRADE IN MACHINERY AND TRANSPORT EQUIPMENT, OTHER MANUFACTURES, AND ALL OTHER GOODS, JANUARY-SEPTEMBER 1964[1]

(In millions of U.S. dollars)

	Trade of				
	United Kingdom	EEC Countries	United States[2]	Other EFTA Countries[3]	Japan
Imports (c.i.f.)					
Machinery and transport equipment	1,137	6,162	1,475	3,385	594
Other manufactures	3,061	10,686	5,026	4,514	899
Food, materials, fuel, etc.	7,313	16,252	7,158	3,845	4,418
Exports (f.o.b.)					
Machinery and transport equipment	3,838	10,240	6,823	2,169	1,310
Other manufactures	3,521	14,062	5,289	4,081	3,071
Food, materials, fuel, etc.	1,452	6,648	5,544	2,984	230

Sources: See Table 17.
[1] Commodity groupings as in Table 16.
[2] Imports f.o.b. Export figures exclude special categories.
[3] Including Finland.

TABLE 19. EEC COUNTRIES: IMPORTS OF MANUFACTURES FROM EACH OTHER AND FROM THE UNITED STATES, JANUARY-SEPTEMBER 1964

Imports of	Value *(million U.S. dollars)*	Percentage Increase over Jan.-Sept. 1963
Machinery and transport eqt.		
From EEC countries	3,642	14.3
From United States	1,089	15.5
Other manufactures		
From EEC countries	6,095	21.6
From United States	979	20.6

Source: Statistical Office of the EEC, *Monthly Foreign Trade Statistics*, 1964, No. 1, and 1965, No. 2.

and the slower growth in U.K. exports, illustrated in Table 17, were strongly influenced by demand conditions in the home and export markets and by other nonprice factors. Nevertheless, the changes in the unit value indices for manufactured exports shown in Table 20 suggest that the disparities between these rates of growth were associated with an apparent improvement in the competitiveness of the former countries' export prices and a further deterioration in those of the United Kingdom. These figures, however, must be interpreted with caution, as was stressed in last year's Annual Report.[1] Between 1962 and 1964, the price competitiveness of German exports of manufactured goods appears to have improved about as much as that of U.S. goods. During the same period the export prices for manufactured goods of France, Italy, Sweden, and Switzerland apparently rose as much as, or more than, those of U.K. manufactures.

[1] See *Annual Report, 1964,* "Supplementary Note C, Export Performance of Manufacturing Countries," especially pages 128-29.

Export Growth and Market Growth

In 1963 there was no very marked divergence in the rate of export expansion which each manufacturing country would have achieved if it had maintained its share of total exports from manufacturing countries to each of 22 market areas; under these conditions every country's exports would have expanded by 8-10 per cent over their 1962 value. By contrast, in 1964 there was a range of market growth over 1963 varying from 10 per cent for Austria to 17 per cent for Norway and 15 per cent for Belgium and Sweden—the last three countries all being considerably dependent on the U.K. market where (as described above) import demand rose rapidly.

TABLE 20. MANUFACTURING COUNTRIES: CHANGES IN THE RELATION BETWEEN EACH COUNTRY'S EXPORT UNIT VALUE AND THE AVERAGE UNIT VALUE OF OTHER COUNTRIES' EXPORTS, 1963-64

	Percentage Changes[1]			
	1962 to 1963		1963 to 1964	
Relative improvement	Germany	—2.5	Japan	—2.0
	Japan	—2.0	United States	—1.0
	United States	—2.0	Italy	—1.0
	Belgium-Luxembourg	—1.0		
	Netherlands	—1.0		
Little change	France	—	Belgium-Luxembourg	—
			Germany	—
Relative deterioration	Sweden	1.0	Netherlands	1.0
	United Kingdom	1.0	United Kingdom	1.0
	Switzerland	3.0	France	2.0
	Italy	4.0	Sweden	2.0
			Switzerland	3.0

Source: Based on unit value indices for manufactured goods published in United Nations, *Monthly Bulletin of Statistics.*
[1] Percentage change in ratio of each country's index of unit value of manufactured goods exports (in U.S. dollars) to combined index for other manufacturing countries for which such data are available. No figures exist for Austria, Denmark, or Norway.

The comparison of market growth and actual export expansion from 1963 to 1964 made in Table 21 may be summed up as follows: Japan and the United States succeeded in increasing substantially their shares of markets; to a large extent the counterpart of their success was the failure of the United Kingdom to maintain its share of markets. The majority of the EEC countries broadly maintained their shares of markets, but Italy and the Netherlands increased their shares. The United Kingdom's loss of market shares was concentrated in a few areas, especially Australia, New Zealand, and South Africa (where both the United States and Japan greatly increased their shares of trade), the U.S. market (where Japan achieved a large part of its gains), and Germany and France (where the share of the EEC countries in trade increased).

TABLE 21. MANUFACTURING COUNTRIES: ACTUAL GROWTH IN EACH COUNTRY'S EXPORTS RELATED TO AVERAGE GROWTH IN ITS EXPORT MARKETS, 1962-64[1]

(Percentage change from preceding year)

	1962		1963		1964	
	Market growth	Export growth	Market growth	Export growth	Market growth	Export growth
Countries which increased their shares of markets from 1963 to 1964						
Japan	10	16	9	11	14	22
United States[2]	3	4	8	7	12	14
Italy	8	12	9	8	14	17
Netherlands	8	7	9	8	15	17
Norway	7	4	8	10	17	20
Countries which broadly maintained their shares of markets from 1963 to 1964						
Austria	10	5	10	5	10	9
Belgium-Luxembourg	9	10	9	12	15	15
France	11	2	8	10	11	11
Germany, Fed. Rep.	8	5	10	10	13	12
Sweden	6	7	8	10	15	15
Countries which failed to maintain their shares of markets from 1963 to 1964						
Denmark	9	9	8	14	14	11
Switzerland	8	10	10	9	13	10
United Kingdom	7	3	9	7	12	4

Sources: Based on data in International Monetary Fund and International Bank for Reconstruction and Development, *Direction of Trade*, and in United Nations, *Monthly Bulletin of Statistics*.

[1] For the purpose of this analysis the world has been divided into 23 markets, consisting of the 13 manufacturing countries, 9 groups of primary producing countries, and the Sino-Soviet area. The rate of growth in the market confronting each exporting country is taken to be the growth in each market weighted according to the share of the country's exports taken by each market in the preceding year. Except for the Soviet area, the growth in the market is taken to be the growth in exports to the area from the manufacturing countries. The actual growth in each country's exports to the Sino-Soviet area has been included as a factor in the average growth of its export markets.

[2] Nonmilitary exports.

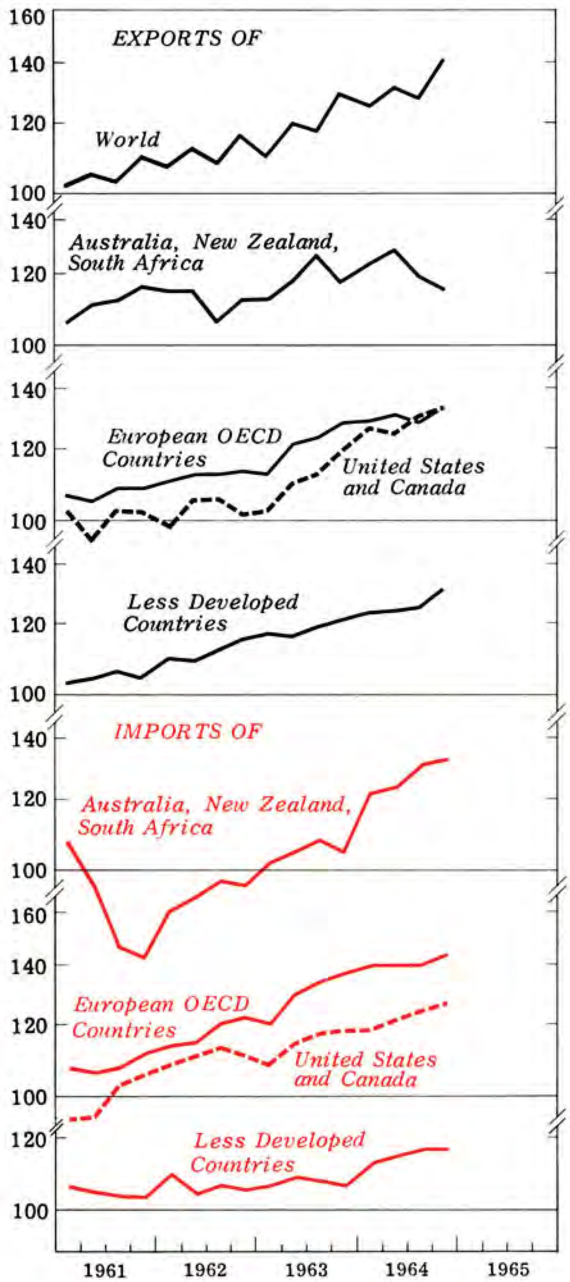
Development of World Trade During 1964

In the course of 1964, a marked difference developed in the trends of export prices of manufacturing countries and of primary producing countries. In the last quarter of 1964 the export unit values of manufacturing countries, except Japan, were higher than the average for the whole year, but those of most primary producing countries declined somewhat (Table 12, p. 53).

Although the growth of world trade from 1963 to 1964 was greater than that from 1962 to 1963, there was actually a slowing down in the rate of expansion during 1964. As Chart 19 illustrates,

CHART 19. VOLUME OF WORLD EXPORTS AND SEASONALLY ADJUSTED VOLUME OF EXPORTS AND IMPORTS OF FOUR MAJOR AREAS, QUARTERLY, 1961-64

(1960 = 100)

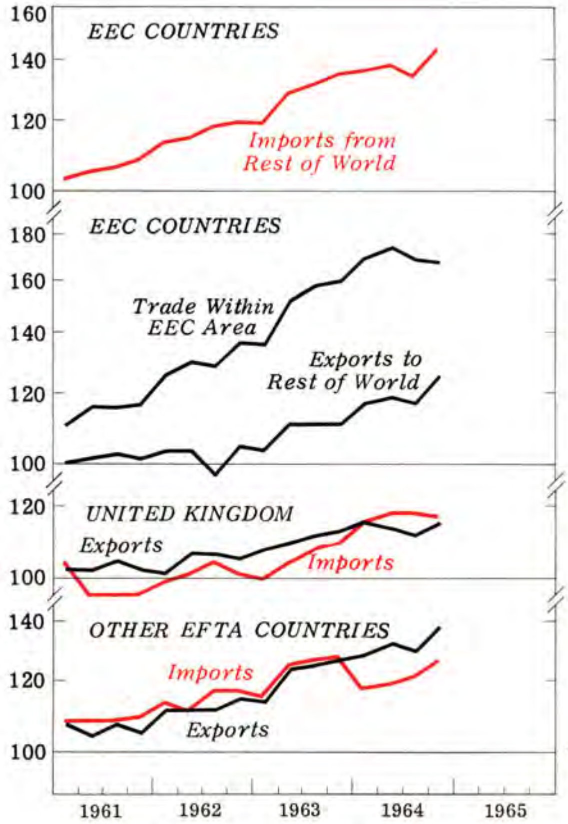


the volume of world exports in the last quarter of 1964 was some 7 per cent higher than a year earlier, following an 11 per cent increase between the last quarters of 1962 and 1963. The slowing down occurred principally in Western Europe's trade, particularly its imports. The volume of imports of the European OECD countries in the last quarter of 1964 was only about 4 per cent higher than a year earlier, in contrast to an increase of 11½ per cent between the final quarters of 1962 and 1963; the corresponding increases in the volume of exports were 5 per cent and 10 per cent, respectively. On the other hand (again comparing growth between the last quarters of the years), there was a somewhat greater expansion in the volume of imports into the United States and Canada, and a considerably greater expansion in the volume of imports of Australia, New Zealand, South Africa, and the less developed countries, during 1964 than during 1963. The export section of the chart indicates that although a slowing down of export growth was common to both the North American and Western European groups, exports from the United States and Canada continued to expand more rapidly than those of Western Europe, as they had done, in volume terms, since the second quarter of 1963. In striking contrast to the upward trend of imports into Australia, New Zealand, and South Africa, the volume of these countries' exports declined in the latter part of 1964. The increase in the volume of the exports of the less developed countries between the second half of 1963 and the second half of 1964 was greater than that between the same periods of 1962 and 1963.

Chart 20 illustrates the development of some major segments of Western Europe's trade. It shows that the slowing down in the growth of the area's imports indicated in Chart 19 reflected (1) a similar change in the imports of the EEC countries from the rest of the world until the final quarter of the year, (2) the interruption of the expansion of trade within the Community in the third quarter, (3) the leveling off of the volume of U.K. imports after the second quarter, and (4) a decline in the volume of other EFTA countries' imports between 1963 and 1964. EEC countries' exports to the rest of the world increased little in volume terms until the final quarter of the year.

CHART 20. EEC COUNTRIES, UNITED KINGDOM, AND OTHER EFTA COUNTRIES: VOLUME OF TRADE, SEASONALLY ADJUSTED, QUARTERLY, 1961-64

(1960 = 100)

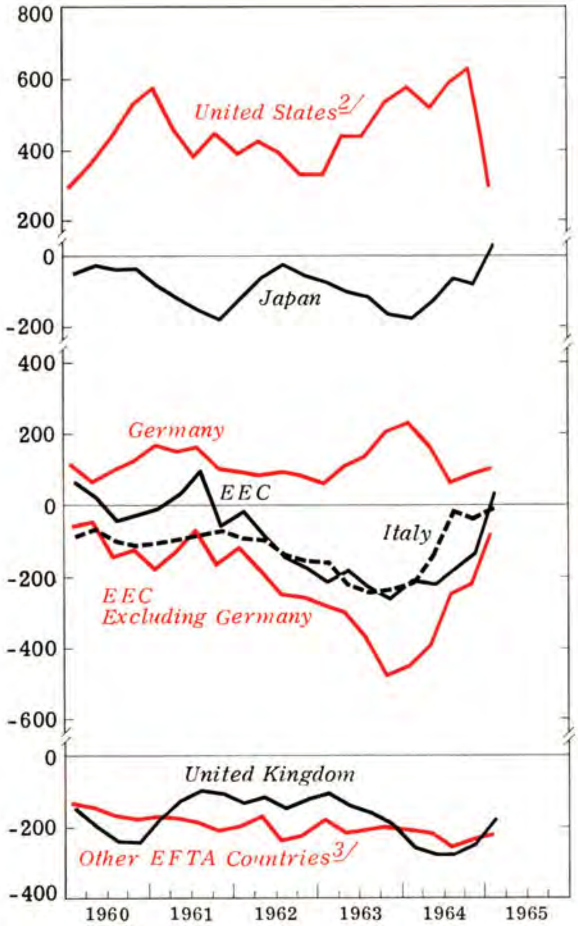


The exports of the other EFTA countries, however, showed a strongly rising trend.

As Chart 21 shows, there was a lessening of the imbalance in various countries' external trade during 1964. Seasonally adjusted, the large combined deficit of the EEC countries other than Germany was steadily reduced in the course of the year, and the German trade surplus (measured imports c.i.f., exports f.o.b.) was about $630 million smaller in the second half of 1964 than at its peak in the second half of 1963. An exception to the general improvement was the United Kingdom, but the deterioration in the U.K. trade balance which had continued throughout 1963 was slower during most of 1964 and was halted in the last quarter of the year. The trade surplus of the United States was rising almost continuously during 1963 and 1964. It was higher in the final quarter of 1964 than in any other quarter of the last five years. However, the surplus may have

CHART 21. MANUFACTURING COUNTRIES: SEASONALLY ADJUSTED TRADE BALANCES, 1961–FIRST QUARTER 1965[1]

(Monthly averages in millions of U.S. dollars)



[1] For the United States, both exports and imports are f.o.b.; for all other countries, exports are f.o.b. and imports are c.i.f. The trade balances in the first quarter of 1965 are strongly influenced by the effects of the U.S. dock strike.

[2] Exports exclude military shipments; imports refer to general imports.

[3] Austria, Denmark, Norway, Sweden, Switzerland.

been somewhat inflated by a speeding up of export deliveries in anticipation of the dock strike. This strike led to a very sharp deterioration in the trade balance in the first quarter of 1965. This change in the U.S. trade balance is, of course, reflected in the improvement of the trade balances of other areas shown in Chart 21, especially for Japan and the EEC. There was a significant improvement in the United Kingdom's balance of trade in the first quarter of 1965, apart from this factor.

Private Capital Movements

In addition to the changes in trade discussed in the preceding section, the major influence on the balance of payments positions of individual countries and areas was exercised by movements of private capital. This section summarizes the broad changes in movements of private capital from 1963 to 1964. However, in 1964, as in other years, the pattern of capital movements was much more difficult to ascertain than changes in trade. Records of capital transactions are less complete and accurate than those of current transactions, and the data reported on capital transactions by different countries do not make up a fully consistent world picture. One difficulty, which applies especially to short-term capital movements, is that of determining the final destination of capital exports, and the initial origin of capital imports, passing through internationalized markets such as the Euro-dollar market.

Among the major events in international capital movements in 1964 were the following:

(1) A rise of about \$1.8 billion in the net outflow of U.S. private capital (see Table 22), of which about two thirds derived from short-term capital. This change was reinforced by a reduction in the inflow of foreign long-term capital into the United States, but the total adverse change of \$2.0 billion on these accounts was partly offset by an increase of \$900 million in the inflow of foreign short-term capital, including liquid funds held mainly by foreign commercial banks.

(2) A rise of about \$500 million in the net outflow of private long-term capital from the United Kingdom. About half of this rise was offset by an opposite change in movements of short-term capital (see Table 32, p. 83).

(3) A reduction of almost \$400 million in the inflow of private long-term capital into Japan, reinforced by a reduction of about \$200 million in the inflow of short-term capital (see Table 36, p. 90).

It is much more difficult to determine which countries benefited from an increase in inflows, or a reduction in outflows, of private capital between 1963 and 1964. U.S. and U.K. statistics suggest an increase of about $1.4 billion in the net export of private capital by these two countries to primary producing countries other than Canada, but the preliminary statistics of those primary producing countries show a much smaller increase.

TABLE 22. NET OUTFLOWS OF PRIVATE U.S. CAPITAL[1]

(In millions of U.S. dollars)

	1963	1964	1964 First quarter	1964 Second quarter	1964 Third quarter	1964 Fourth quarter
Direct Investment						
Western Europe	−924	−1,342	−288	−382	−303	−369
Canada	−365	−250	−66	39	−15	−208
Other Western Hemisphere	−236	−290	−38	−88	−64	−100
Japan	−68	−73	−30	−12	−18	−13
Other	−383	−421	2	−163	−40	−220
Total	−1,976	−2,376	−420	−606	−440	−910
Other Long-Term						
Western Europe	−750	−520	−93	−76	−83	−268
Canada	−547	−668[2]	−41	−186	−91[2]	−350
Other Western Hemisphere	9	−344	−43	−43	−56	−202
Japan	−304	−117	−44	−15	−18	−40
Other	−98	−122	−33	−15	−50	−24
Total	−1,690	−1,771	−254	−335	−298	−884
Short-Term						
Western Europe	−87	−375	−18	−242	−14	−101
Canada	−6	−395	−254	−157	77	−61
Other Western Hemisphere	−110	−604	−60	−95	−175	−274
Japan	−467	−522	−237	−70	−41	−174
Other	−115	−215	−56	−33	−49	−77
Total	−785	−2,111	−625	−597	−202	−687
Total						
Western Europe	−1,761	−2,237	−399	−700	−400	−738
Canada	−918	−1,313	−361	−304	−29	−619
Other Western Hemisphere	−337	−1,238	−141	−226	−295	−576
Japan	−839	−712	−311	−97	−77	−227
Other	−596	−758	−87	−211	−139	−321
Total	−4,451	−6,258	−1,299	−1,538	−940	−2,481

Source: Department of Commerce, *Survey of Current Business*, June 1965.

[1] No sign indicates net inflow; minus sign indicates net outflow.

[2] U.S. published figures have been adjusted to exclude that portion of the Columbia River Consortium payment to Canada that was converted by the Canadian Government into nonmarketable U.S. Government securities.

U.S. statistics show an increase of about $400 million in the net flow of capital into Canada, in the form of U.S. capital moving to Canada minus Canadian long-term capital moving to the United States. Canadian statistics show a rise of only about $100 million in the total inflow of short-term and long-term capital from all countries. The difference between the two figures, which results in part from the different treatment of flows of Canadian short-term capital (which are included in the Canadian statistics) and from purely statistical discrepancies, may also reflect movements of U.S. short-term capital to European financial markets that have been recorded in U.S. statistics as directed toward Canada.

For the European Economic Community there appears to have been a rise of $1.5 billion in the total inflow of private long-term and short-term capital other than changes in commercial bank assets and liabilities (Table 23). This, however, was offset by an almost equivalent and opposite change from a large inflow to a small outflow on account of commercial bank assets and liabilities, reflecting for the most part the change from net borrowing to net repayments by Italian commercial banks that took place under a series of directives by the Italian monetary authorities. However, net inflows of private capital into other industrial countries in Europe appear to have risen by almost $400 million from 1963 to 1964 (Table 24).

In the year as a whole, while movements of private capital were in many cases disequilibrating, there were few examples of disruptive capital movements attributable to speculation. For instance, there was in the aggregate an apparent net inflow of short-term capital into the United Kingdom, even though there was a very large outflow in the last quarter. While there was probably a considerable speculative outflow of capital from Italy in the first quarter of 1964, there appears to have been during the remainder of the year a return of funds that was at least as large. The outflow of short-term capital from the United States was substantial in all quarters of 1964, except the third, but there is no evidence that it was greatly influenced by speculation; almost half of the increase in this outflow was directed to nonindustrial countries. There is also little evidence of large inflows of capital attributable to speculation in continental Europe during 1964 as a whole, perhaps in part because the net inflows of capital into that area were moderated by official measures in several countries.

Nevertheless, it is apparent that the pattern of capital movements that developed during 1964 was not consistent with equilibrium in the balances of payments of several major countries, and that in particular a reduction in the net out-

TABLE 23. EEC COUNTRIES: BALANCE OF PAYMENTS SUMMARIES, 1963 AND 1964[1]

(In millions of U.S. dollars)

		Goods, Services, and Private Transfers (1)	Official Transfers and Capital[2] (2)	Other Nonmonetary Long-Term Capital (3)	Extraordinary Transactions[3] (4)	Basic Balance (Col. 1+2+3 minus Col. 4) (5)	Other Nonmonetary Short-Term Capital and Errors and Omissions (6)	Net Commercial Bank Short-Term Assets[4] (7)	Net Reserves[4, 5] (8)
Belgium-Luxembourg	First Half 1963	32	34	14	2	78	—	58	—138
	Second Half 1963	—66	—42	16	2	—94	4	154	—66
	Total	—34	—8	30	4	—16	4	212	—204
	First Half 1964	—56	8	48	—	—	14	4	—18
	Second Half 1964	102	—26	114	—	190	12	36	—238
	Total	46	—18	162	—	190	26	40	—256
France[6]	First Half 1963	342	—143	290	—61	550	59	135	—683
	Second Half 1963	194	—311	226	—220	329	—3	67	—173
	Total	536	—454	516	—281	879	56	202	—856
	First Half 1964	—2	—76	253	—	175	197	57	—429
	Second Half 1964	44	—69	279	—	254	151	—19	—386
	Total	149	—145	548	—	552	225	38	—815
Germany, Fed. Rep. of	First Half 1963	307	—307	270	6	264	337	—361	—246
	Second Half 1963	751	—546	195	30	370	—463	532	—469
	Total	1,058	—853	465	36	634	—126	171	—715
	First Half 1964	859	—669	—81	6	103	527	—451	—185
	Second Half 1964	32	—618	168	28	—446	—14	464	—32
	Total	891	—1,287	87	34	—343	513	13	—217
Italy	First Half 1963	—397	—23	—183	—	—603	—76	536	143
	Second Half 1963	—229	—41	—103	—	—373	—200	114	459
	Total	—626	—64	—286	—	—976	—276	650	602
	First Half 1964	—406	—52	230	—	—228	18	—344	554
	Second Half 1964	1,091	41	172	—	1,304	—317	—98	—889
	Total	685	—11	402	—	1,076	—299	—442	—335
Netherlands	First Half 1963	—71	—21	47	1	—46	68	64	—87
	Second Half 1963	153	—42	—63	—68	116	72	—37	—83
	Total	82	—63	—16	—67	70	140	27	—170
	First Half 1964	—368	—20	—1	1	—390	91	209	89
	Second Half 1964	205	—11	117	1	310	48	—21	—338
	Total	—163	—31	116	2	—80	139	188	—249
Grand Total	First Half 1963	213	—460	438	—52	243	388	432	—1,011
	Second Half 1963	803	—982	271	—256	348	—590	830	—332
	Total	1,016	—1,442	709	—308	591	—202	1,262	—1,343
	First Half 1964	27	—809	449	7	—340	847	—525	11
	Second Half 1964	1,474	—683	850	29	1,612	—120	362	—1,883
	Total	1,501	—1,492	1,299	36	1,272	727	—163	—1,872

Source: Based on data reported to the International Monetary Fund. For 1964, the data for some countries are provisional and are not entirely comparable with those for 1963.

[1] No sign indicates credit; minus sign indicates debit.

[2] Excluding capital movements considered as reserve movements; see footnote 5.

[3] Included in column 2; mainly advance debt repayments, but include also all repayments on post-EPU debts.

[4] Increase (—).

[5] Reserve movements generally cover changes in official holdings of gold and foreign exchange assets, in short-term liabilities of the central monetary sector, and in IMF position. Repayments on post-EPU claims and debts are included with official transfers and capital.

[6] Transactions of overseas franc area settled through Metropolitan France are included with Other Nonmonetary Short-Term Capital. For 1964, half-yearly figures do not add to annual total since certain adjustments made to the latter are not yet distributable between half years.

flow of capital from the United States and the United Kingdom was needed. The outflow of capital from the United States and the United Kingdom continued on a considerable scale in the early months of 1965, and both countries took measures to reduce their capital exports. The programs adopted by these countries to adjust their balances of payments are discussed in Chapter 8. Developments in international capital markets and in long-term and short-term interest rates are reviewed in Chapter 5.

TABLE 24. OTHER MANUFACTURING COUNTRIES IN CONTINENTAL EUROPE: BALANCE OF PAYMENTS SUMMARIES, 1963 AND 1964[1]

(In millions of U.S. dollars)

		Goods, Services, and Private Transfers	Official Transfers and Capital[2]	Other Non-monetary Long-Term Capital	Other Non-monetary Short-Term Capital and Errors and Omissions	Net Commercial Bank Short-Term Assets[3]	Net Reserves[3,4]
Austria	1963	21	—	89	72	—46	—136
	1964	—4	36	37	15	—2	—82
Denmark	1963	30	29	146	37	—27	—215
	1964	—196	23	96	185	60	—168
Norway	1963	—186	32	202	12	—9	—51
	1964	—67	32	120	—29	—17	—39
Sweden	1963	—38	—14	—52	89	—29	44
	1964	1	—2	24	170	7	—200
Switzerland	1963	—360	15	—139[5]	540[5]	...	—56
	1964	—460	93	—80[5]	660[5]	...	—213
Total	1963	—533	62	246	750	—111	—414
	1964	—726	182	197	1,001	48	—702

Source: Based on data reported to the International Monetary Fund. For 1964, the data for some countries are provisional and are not entirely comparable with those for 1963.

[1] No sign indicates credit; minus sign indicates debit.

[2] Excluding capital movements considered as reserve movements; see footnote 4.

[3] Increase (—).

[4] Reserve movements generally cover changes in official holdings of gold and foreign exchange assets, in short-term liabilities of the central monetary sector, and in IMF position. Repayments on post-EPU claims and debts are included with official transfers and capital.

[5] Covers only issues and redemptions of foreign bonds in Switzerland. Other private long-term capital is included indistinguishably in errors and omissions.

Balance of Payments Developments

Current Account and "Basic" Balances

The changes in the trade balances of the various countries and areas from 1963 to 1964, and during each of these years, provide much of the explanation of the changes in the net positions on total current account, defined here as the balance on account of goods and services and private transfer payments. The main changes between 1963 and 1964 were the following (see Chart 22; in the discussion of movements within each year, allowance is made as far as possible for seasonal factors):

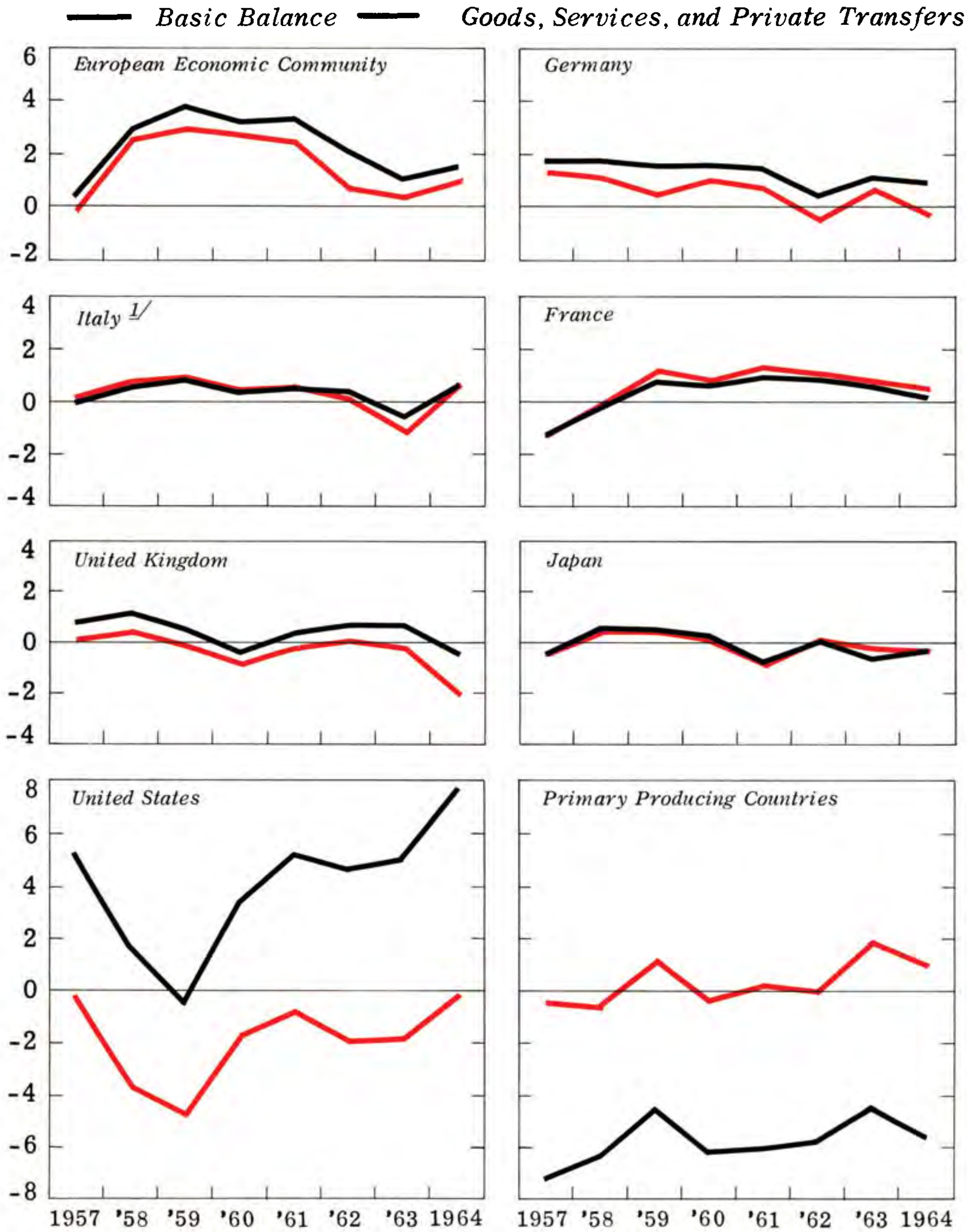
(1) A sharp rise (of $2.6 billion) in the current surplus of the United States, to a record figure of $7.7 billion. This was largely a result of developments prior to the first quarter of 1964; during the remainder of that year, the surplus did not change much.

(2) A shift, by about $1.2 billion, from a current surplus to a current deficit in the balance of payments of the United Kingdom. Most of the deterioration had taken place by the first quarter of 1964, although the low point was not reached until the third quarter.

(3) A rise of about $500 million in the current surplus of the EEC countries. This resulted exclusively from developments during 1964. Indeed, the current surplus of the area fell sharply during 1963 and reached a low point in the last quarter of that year, after which it rose even more sharply.

CHART 22. SELECTED AREAS AND COUNTRIES: BALANCES OF PAYMENTS, 1957-64

(In billions of U.S. dollars)



[1] Basic balance includes errors and omissions and small amounts of nonmonetary sector short-term capital.

(4) A reduction of about $300 million in the current deficit of Japan. The deficit rose during 1963 and reached its maximum in the first quarter of 1964, but was replaced by a surplus in the second half of the year.

(5) A rise of about $1.1 billion in the current deficit of the primary producing countries, as a group. The absence of seasonally adjusted trade figures for this group makes it difficult to determine the exact turning point between the improvement in the current balance that took place during most of 1963 and the deterioration that took place during most of 1964.

(6) An increase of about $0.2 billion in the aggregate current account deficit of EFTA countries other than the United Kingdom.

The changes in the current balances of the United Kingdom, Japan, and the EEC countries, in particular, are closely related to the developments in the domestic economies of the countries concerned, which are reviewed in Chapter 5. The net movement in the current balance of the EEC area as a whole is the product of rather diverse movements in the balances of individual member countries, particularly those of Germany, Italy, and France. Balance of payments developments in these countries are noted in Chapter 8. The current balances of France (with countries outside the French franc area) and Germany deteriorated from 1963 to 1964, but the change from a large deficit to a large surplus in Italy's current transactions was much greater than the opposite changes in the current balances of the other countries. The current balance of the Netherlands also deteriorated, while that of Belgium-Luxembourg showed a small improvement. The sharp rise in the area's current surplus between the first and second halves of 1964, too, was dominated by the swing in Italy's balance of payments, which was reinforced by seasonal factors. During that period all the EEC countries, except Germany, improved their current balances (see Table 23). The extent to which seasonal factors affect the balances of payments of individual members of the area is not known precisely, but it is apparent that the rise in the current surplus from the first to the second half of 1964 must include a considerable seasonal element. In 1963, when the current surplus of the area also rose between the first and second half of the year, the seasonally adjusted trade balance moved in the opposite direction. A comparison of the figures for the second halves of 1963 and 1964 suggests that the intervening rise in the area's current account surplus was of the order of $1.4 billion, at an annual rate.

It is thus apparent that the reduction in the current surplus of the EEC area that began in 1961 was interrupted during 1964. Certainly, much of the rise in the area's surplus in 1964 is accounted for by Italy, whose surplus early in 1965 seems likely to be gradually reduced as a result of the measures introduced late in 1964 and early in 1965 to reactivate the country's economy. However, since there is a close relationship between the balances of payments of the individual members of the area, the resulting reduction in the area's current surplus would presumably be much smaller. Some reduction in the area's current surplus might also be induced by an upswing in the French economy later in 1965. It is not clear what further reduction in the area's current surplus, from the high rate reached in the second half of 1964, would be required to restore equilibrium in the area's over-all balance of payments. For 1964 as a whole, the area's current surplus was equal to the outflow on account of government transfer payments and capital transactions, and the area's over-all surplus was about equivalent to the net inflow of private capital. If the inflow of private capital into the area should be reduced, as seems a likely consequence of the program recently adopted by the U.S. Government to reduce the outflow of U.S. capital, and if private capital exports from the area should increase, the reduction in the current surplus needed to restore equilibrium in the area's over-all balance of payments might be rather limited.

As one indicator of the degree of imbalance in international transactions, Chart 22 shows so-called basic balances (balances on account of current and long-term capital transactions, excluding advance repayments on government debt) for major countries and areas for 1957-64, together with their current balances. While the picture presented by this analysis is rather mixed, it is apparent that the general progress toward a balanced pattern of international transactions that was recorded in 1963 was not continued in 1964. One helpful development, however, was that the basic deficit of the United States was reduced to a very low figure in 1964. This reduction, in contrast to that which occurred during 1959-61, has coincided with vigorous growth in the domestic economy. It has resulted from two opposite movements: a considerable rise in the current surplus, partly offset by larger outflows of capital.

A change in the direction of greater imbalance was the rise in the basic surplus of the EEC area, much of which was due to the very sharp improvement in Italy's balance of payments in 1964. The extent to which this improvement relates to long-term capital transactions is difficult to ascertain, and most likely it is somewhat overstated in Chart 22—as is, therefore, the rise in the basic surplus of the EEC as a whole. This rise occurred after the first quarter of 1964, and at the end of the year the basic surplus was running at a higher rate than the average for the year.

Other major changes in basic balances between 1963 and 1964 took place in the United Kingdom and in the primary producing countries as a group. The basic balance of the United Kingdom changed from near equilibrium to a large deficit as a result of the deterioration of the current account in combination with the rise in the net outflow of long-term capital, discussed above. The reduction in the aggregate basic surplus of the primary producing countries was due mainly to a rise in the deficit on goods and services account; developments in the trade and balances of payments of these countries are reviewed in the next chapter.

Over-All Surpluses and Deficits

Table 25 presents estimates of over-all surpluses or deficits for all countries for which balance of payments statistics are available, based on a broadly symmetrical definition. A surplus or deficit is defined as the balance of all transactions other than "official settlements" (i.e., excluding changes in official gold and foreign exchange assets, in net IMF positions, and in liabilities to foreign monetary authorities, and adjusted for advance repayments of foreign debt by governments). The over-all surplus or deficit so defined is equal to the basic balance, unrecorded transactions, and all movements of short-term capital, excluding only those that constitute official settlements. The application of this concept to the U.S. balance of payments is discussed in Chapter 8.

In general, the changes between 1963 and 1964 in over-all balances, so defined, were in the same direction as those in basic balances. Thus the U.S. deficit fell by about $1 billion; this was, however, considerably less than the reduction in the basic deficit, since there was an increase of more than $900 million in the net outflow on account of U.S. and foreign short-term capital and unrecorded transactions (Item E of Table 30, p. 80). The over-all surplus of the EEC area rose a few hundred million dollars less than its basic surplus as a result of the change in movements of commercial bank assets and liabilities (mainly Italian) referred to above, since there was a rise in the inflow of other short-term capital into the area (see Table 23). The over-all deficit of the United Kingdom rose by about $1.4 billion, a few hundred million dollars less than the rise in the basic deficit, movements of short-term capital (plus unrecorded transactions) being more favorable in 1964 than in 1963 (see Table 32, p. 83).

The other manufacturing countries in Europe increased their over-all surplus by $290 million (Table 24). Although this was due to increased inflows of capital (the aggregate current deficit of these countries rose by about $200 million), it would apparently not have occurred had it not been for the large deficit in the balance of payments of the United Kingdom and the increase in exports to that country with which this deficit was associated. This group of countries and the more industrialized primary producing countries together increased their aggregate reserves in each of the years 1963 and 1964 by about $1.5 billion. This is more than twice the average annual addition to world monetary gold holdings during the past decade, which is the amount by which total surpluses can normally exceed total deficits. The aggregate surplus of the less industrialized primary producing countries, which had reached approximately $1 billion in 1963, fell to about $200 million in 1964.

The comparison of over-all surpluses and deficits in 1964 as a whole with those in 1963 fails to reveal the major deterioration that took place in international payments last year. At the beginning of 1964, the over-all positions of both the United States and the EEC area were close to equilibrium. In the second half of the year, however, a major U.S. deficit and a major surplus for the Community reappeared. Moreover, the over-all deficit of the United Kingdom remained moderate during the first half of the year (when a large part of the basic deficit was matched by an inflow of short-term capital); but a net outflow of short-term capital raised the U.K. deficit to a very large amount in the second half of the year, particularly in the last

TABLE 25. OVER-ALL BALANCES OF INTERNATIONAL PAYMENTS, 1963 AND 1964[1]

(In millions of U.S. dollars)

	1963			1964		
	First half	Second half	Year	First half	Second half[2]	Year[2]
A. Countries exporting mainly manufactured products						
United States	—1,421	—859	—2,280	—88	—1,243	—1,331
United Kingdom	—133	—347	—480	—261	—1,610	—1,871
European Economic Community countries	1,028	621	1,649	—80	1,946	1,866
Belgium-Luxembourg	*122*	*65*	*187*	*—4*	*242*	*238*
France	*705*	*436*	*1,141*	*376*	*447*	*823*
Germany, Federal Republic of	*254*	*437*	*691*	*205*	*23*	*228*
Italy	*—143*	*—453*	*—596*	*—564*	*894*	*330*
Netherlands	*90*	*136*	*226*	*—93*	*340*	*247*
Austria	25	122	147	—8	97	89
Denmark	60	155	215	44	131	175
Norway	52	—1	51	14	19	33
Sweden	—10	—33	—43	54	151	205
Switzerland	—164	367	203	—122	248	126
Japan[3]	283	—22	261	—171	132	—39
Total, Group A	—280	3	—277	—618	—129	—747
B. Countries exporting mainly primary products						
Australia	115	378	493	133	—66	67
Canada	155	—18	137	24	313	337
Finland	—14	44	30	33	29	62
New Zealand	65	—94	—29	103	—80	23
Portugal	—24	59	35	22	90	112
South Africa	79	40	119	—23	—40	—63
Spain	—15	116	101	117	266	383
Subtotal, more industrialized countries	361	525	886	409	512	921
Latin American Republics	49	318	367	141	165	306
Argentina	*44*	*100*	*144*	*—4*	*—67*	*—71*
Brazil	*—82*	*16*	*—66*	*—73*	*151*	*78*
Mexico	*14*	*122*	*136*	*34*	*77*	*111*
Venezuela	*52*	*104*	*156*	*39*	*55*	*94*
Other	*21*	*—24*	*—3*	*145*	*—51*	*94*
Miscellaneous sterling countries	154	—21	133	25	—147	—122
Other Europe	13	29	42	—42	44	2
Other	376	55	431	116	—87	29
Subtotal, less industrialized countries	592	381	973	240	—25	215
Total, Group B	953	906	1,859	649	487	1,136
C. Excess of surpluses	673	909	1,582	31	358	389
1. Due to increase in world monetary gold	*285*	*555*	*840*	*630*	*95*	*725*
2. Due to identifiable asymmetries[4]	*185*	*36*	*221*	*—70*	*—82*	*—152*
3. Due to errors and omissions	*203*	*318*	*521*	*—529*	*345*	*—184*
D. Memorandum items						
United States and Canada	—1,266	—877	—2,143	—64	—930	—994
Continental Europe in Group A	991	1,231	2,222	—98	2,592	2,494
Group B, excluding Canada	798	924	1,722	625	174	799

[1] Adjusted for advance debt repayments. Over-all balances are measured here by changes in official gold and foreign exchange assets, in net IMF positions, in liabilities resulting from "swap" transactions with the United States, and, where data are available, in other short-term liabilities to foreign monetary authorities. This table is based on data on reserves, whereas Table 29 is based on balance of payments reports, which in general cover annual data only. Because of minor differences in the countries covered and between the half-yearly and the annual data, the aggregate "over-all balances" for 1963 and 1964 for the less industrialized primary producers differ slightly from the totals shown in Table 29. No sign indicates surplus; minus sign indicates deficit.
[2] Preliminary.
[3] Adjusted for repayments on short-term credits negotiated by the Japanese authorities in connection with the 1961 balance of payments crisis.
[4] Covers omissions from the table of one side of certain transactions, e.g., contra-entries necessary when Swiss franc proceeds of Roosa Bonds held by the Swiss Government are utilized by the United States in purchases of U.S. dollars from the Swiss National Bank, because both the bonds and the franc liabilities are included "above-the-line" in the Swiss figures; contra-entries to the adjustments to Japan's figures (see footnote 3); and contra-entries for advance debt repayments to international nonmonetary institutions (e.g., the IBRD).

quarter. Early in the year, certain imbalances within the EEC area had been reduced—the large German surplus and large Italian deficit that existed at the beginning of the year had been eliminated. However, the Italian deficit was soon replaced by an equally large surplus.

In the last quarter of the year, the total imbalance in world payments reached a very high figure. Indeed, when measured as the sum of the deficits of all countries in deficit, the total imbalance in world payments in that quarter was the highest ever recorded. This is illustrated in Chart 23, which shows by quarters for the period 1958-64 the aggregate deficit of all countries in deficit, and similar data for industrial and for nonindustrial countries. The very high figure for the last quarter of 1964 reflects mainly the coincidence of large deficits in the balances of payments of the United States and the United Kingdom.

Reserve Developments

The change in the pattern of over-all surpluses and deficits from 1963 to 1964 resulted in a slowing down in the growth of world reserves (Table 26). Aggregate reserves of countries outside the Sino-Soviet area increased by $2.5 billion in 1964. Although this increase was larger than in most postwar years, it was considerably less than the record increase of $3.4 billion in 1963. The smaller increase was associated with a marked reduction in the balance of payments surpluses of the nonindustrial countries. Within this group, the increase in reserves of the more developed countries fell from $0.8 billion to $0.5 billion, while that of less developed countries declined from $1.0 billion to about $0.1 billion. In both years, the growth in total reserves was considerably smaller than that in the value of international transactions, which for the two years combined rose about three times as fast as reserves.

CHART 23. ALL COUNTRIES IN BALANCE OF PAYMENTS DEFICIT: AGGREGATE DEFICIT, 1958–FIRST QUARTER 1965

(In millions of U.S. dollars)

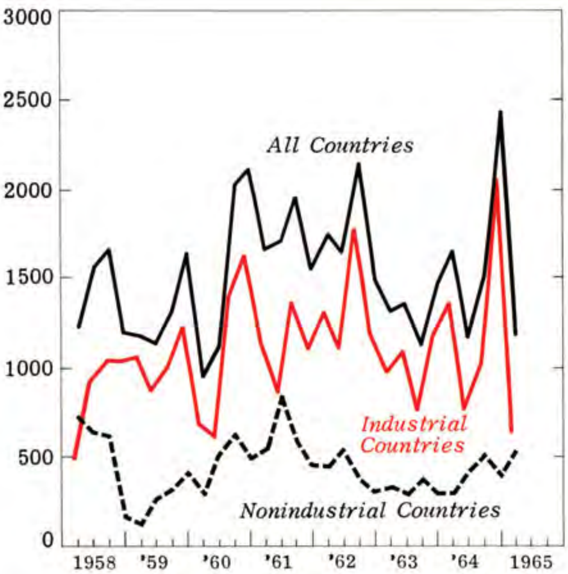


TABLE 26. COUNTRIES' OFFICIAL RESERVES, INCLUDING RESERVE POSITIONS IN THE IMF, END OF CALENDAR YEARS, 1961-64[1]

(In billions of U.S. dollars)

	1961	1962	1963	1964
Countries[2]				
Industrial countries	49.04	48.93	50.55	52.37
United States	*18.75*	*17.22*	*16.84*	*16.67*
United Kingdom	*3.32*	*3.31*	*3.15*	*2.32*
Other[3]	*26.97*	*28.40*	*30.56*	*33.38*[4]
Other developed areas[5]	4.67	5.35	6.18	6.72
Other countries	8.96	8.81	9.78	9.90
Total	62.67	63.09	66.51	68.99
Composition				
Gold	38.89	39.27	40.23	40.86
IMF positions—gold tranche	4.16	3.80	3.94	3.75
—loans under GAB[6]	—	—	—	0.41
Claims on United States[7]	11.98	12.55	13.94	14.94
Claims on United Kingdom[8]	7.10	6.21[9]	6.53	7.05
Other[10]	0.54	1.26	1.87	1.98

Source: International Monetary Fund, *International Financial Statistics,* and staff estimates.

[1] The data for other countries and the totals in the 1964 Annual Report included residual estimates of reserves held by certain countries for which direct reports are not available. These estimates have been excluded here, since it has been ascertained that they refer for the most part to unofficial holdings.

[2] Excluding the Sino-Soviet area.

[3] Austria, Belgium, Canada, Denmark, France, Germany, Italy, Japan, Netherlands, Norway, Sweden, Switzerland.

[4] Includes assets arising from Swiss assistance to the United Kingdom, held by the Swiss Confederation.

[5] Other Western Europe, Australia, New Zealand, and South Africa.

[6] Sums borrowed by Fund under General Arrangements to Borrow.

[7] Covers short-term liquid liabilities to central banks and governments; foreign official holdings of U.S. Government marketable securities; and foreign official holdings of U.S. Government long-term nonmarketable securities for those countries that are believed to include such holdings in their reserves figures.

[8] For 1961, covers net sterling liabilities to foreign official holders; for 1962-64, covers gross liabilities to foreign central monetary authorities, including inter-central-bank assistance.

[9] The change in coverage described in footnote 8 reduces the figure for sterling claims by about $0.6 billion and increases the residual ("other") by the same amount.

[10] Including claims on countries other than the United Kingdom and the United States (including Euro-dollar claims), currency deposits with the Bank for International Settlements, and net errors and omissions.

The addition in 1964 to world monetary gold holdings (including the holdings of international monetary organizations) was $725 million, some $115 million less than in the previous year. Gold production rose again and there was an apparent reduction in hoarding, but Soviet sales were lower than in 1963 (for details see Chapter 9). Country holdings of gold rose by $635 million, or by $90 million less than total monetary gold holdings. This was the result of a net inflow from the Fund of $133 million (IMF gold sales for currencies of $250 million less IMF gold receipts from subscriptions and repurchases of $117 million) and a net outflow of $225 million to the Bank for International Settlements and the European Fund. The chief beneficiaries from the increase in world monetary gold holdings were again the industrial countries other than the United States and the United Kingdom. The gold reserves of this group rose by $1,088 million in 1964. Those of the United States and the United Kingdom fell by $125 million and $348 million, respectively, and the gold reserves of the nonindustrial countries were virtually unchanged.

Of the total increase of $2.5 billion in national reserves, $1,630 million took the form of foreign exchange assets. About two thirds of the increase referred to claims on the United States and about one third to claims on the United Kingdom, the latter representing mainly the use of central bank assistance rather than changes in ordinary sterling reserves. Of the total, the industrial countries added $1,085 million to their reserves, of which $220 million went to the United States and more than $850 million to the other industrial countries except the United Kingdom, whose holdings of foreign exchange were almost unchanged. The nonindustrial countries in 1964 were able to add only $545 million in foreign exchange to their reserves, compared with $1,490 million in 1963, and most of the 1964 addition went to the more developed nonindustrial countries.

The remaining component of reserves—reserve positions with the IMF—was also mainly affected by the transactions of the industrial countries. The change in this component reflected primarily reductions in the positions of the United States and the United Kingdom, resulting from their drawings on the IMF during the year, and the corresponding rise in the IMF positions of the other industrial countries, including those arising from the activation of the General Arrangements to Borrow.

There was a slight reduction in the percentage of total gold and foreign exchange reserves held in gold by the industrial countries other than the United States and the United Kingdom. The main reason was that Italy increased its foreign exchange holdings by $734 million while reducing its gold holdings by $236 million. This, in combination with the gold sales by the United Kingdom, helped to keep the outflow of gold from the United States lower than could have been expected in view of the size of the deficit requiring official settlement, and thus to maintain a higher rate of increase in world reserves than would otherwise have been possible.

During the first quarter of 1965, world reserves declined by about $800 million. Part of this decline is explained by a reduction of about $210 million in world monetary gold holdings, apparently associated with the developments in gold markets reviewed in Chapter 9. Another contributory factor was the conversion of existing foreign exchange balances into gold by certain countries.

Chapter 7

Developments in Countries Exporting Primary Products

THE international demand conditions that countries exporting primary products faced during 1964 and the early part of 1965 were, on the whole, more favorable than they had been for a number of years. The prices of most basic commodities rose late in 1963 and early in 1964 and then remained at, or close to, the levels reached at that time. These relatively high prices reflected generally strong international demand. Consequently, the export receipts of primary product exporting countries tended to rise in the early part of 1964 and to remain relatively stable. Capital flows and grants to the developing countries continued on the same scale, so that the total exchange receipts of these countries were high; as a group, these countries achieved a small increase in international reserves. Most of their increased foreign receipts, however, were directed toward an expansion of imports. This reflected the strong need for these countries to raise their living standards, both directly through higher present consumption and indirectly by more rapid capital investment for future increases in domestic output. In some countries, however, the demand for imports was stimulated by excessive monetary expansion.

Prices

On the average, the prices of primary products in 1964 were 5 per cent higher than in 1963 and, in general, higher than they had been in any of the eight previous years. On the other hand, because of rising import prices, the terms of trade of primary producing countries improved only slightly. If sugar prices, which fell sharply after their steep advance in 1963, are excluded, the increase over the 1963 average was as much as 7 per cent, against 4 per cent between 1962 and 1963. However, as indicated in Table 27 and Chart 24, this rise in the average in 1964 resulted from rather sharp increases starting in late 1963 and continuing into early 1964, followed by relative stability and even some declines, which were most marked for agricultural raw materials. Metal and mineral prices continued to rise during the year. As shown in Chart 25, 1964 was marked by widespread price increases; however, in the latter half of the year they were generally less dramatic than they had been earlier.

Prices for foodstuffs, excluding sugar but including the beverage crops, reached a peak in the first half of 1964 and declined thereafter. These

TABLE 27. COUNTRIES EXPORTING PRIMARY PRODUCTS: INDICES OF COMMODITY PRICES[1]

(1957 = 100)

	1962	1963 First half	1963 Second half	1964 First half	1964 Second half	1965 First quarter
Total	88	94	98	102	99	96
Total, excl. sugar	89	92	95	100	100	98
Food, excl. sugar	86	89	93	101	100	99
Raw materials						
Agriculture	83	87	88	91	86	82
Metals and minerals	99	99	101	106	116	115
Sugar (world)	58	148	182	154	74	47

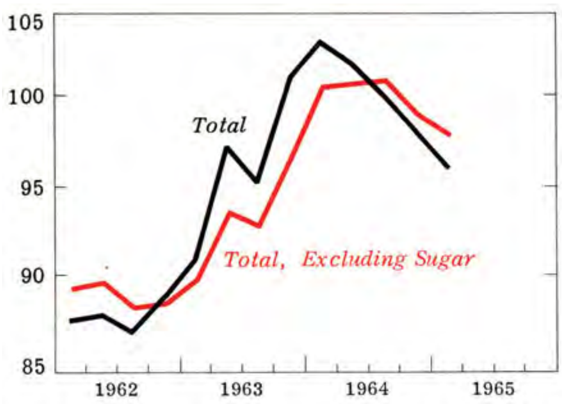
Source: Based on data from *National Institute Economic Review* (London), adjusted for copper by substituting producers' export prices for quotations on the London Metal Exchange.

[1] Excluding petroleum.

movements resulted primarily from variations in actual or anticipated supply, caused chiefly by variations in crops and, to a lesser extent, by support policies in the exporting countries. The sharp downturn in sugar prices in 1964 reflected the recovery of output in 1963-64 and expectations of a further substantial rise in production in the current season. Developments on the cocoa market followed a similar pattern, although they were

CHART 24. PRIMARY PRODUCING COUNTRIES: PRICES OF COMMODITIES EXPORTED (EXCLUDING PETROLEUM), 1962–FIRST QUARTER 1965

(1957 = 100)



considerably less pronounced. The advance in most coffee prices early in 1964 reflected anticipation of a serious crop failure in Brazil; later on, prices were strengthened by the withholding of supplies by some major exporting countries within the framework of the coffee agreement. The price pattern for agricultural raw materials also largely reflected crop variations; for example, a poor crop in the Sudan has been largely responsible for the rise in the prices of long-staple cotton. However, these raw materials—which include textile fibers and rubber—have been affected by the rapidly increasing use of synthetics, which had a dampening effect on the demand for natural products. Metal prices followed a different course; they were largely dominated by a sustained increase in demand, which could not be adequately met by the slow rise in output. The rise in prices started later than that for foods and raw materials but gained momentum and continued through most of the year and into 1965, when continued political tensions served to strengthen demand further. The index quoted in Table 27 reflects prices charged by producers, which for some commodities (most notably copper) were held well below market quotations. This policy, adopted primarily in order to avoid a shift to substitutes, may also prevent a possibly short-lived boom from inducing overexpansion of capacity.

Trade

As indicated in Table 28 (see also Chart 19, p. 58), the export earnings of the primary product exporting countries as a group expanded during 1964 by a larger percentage than in 1963. However, for the countries exporting mainly coffee, other tropical foods, and other agricultural products, the percentage growth in export earnings, although large, was smaller in 1964 than in 1963.

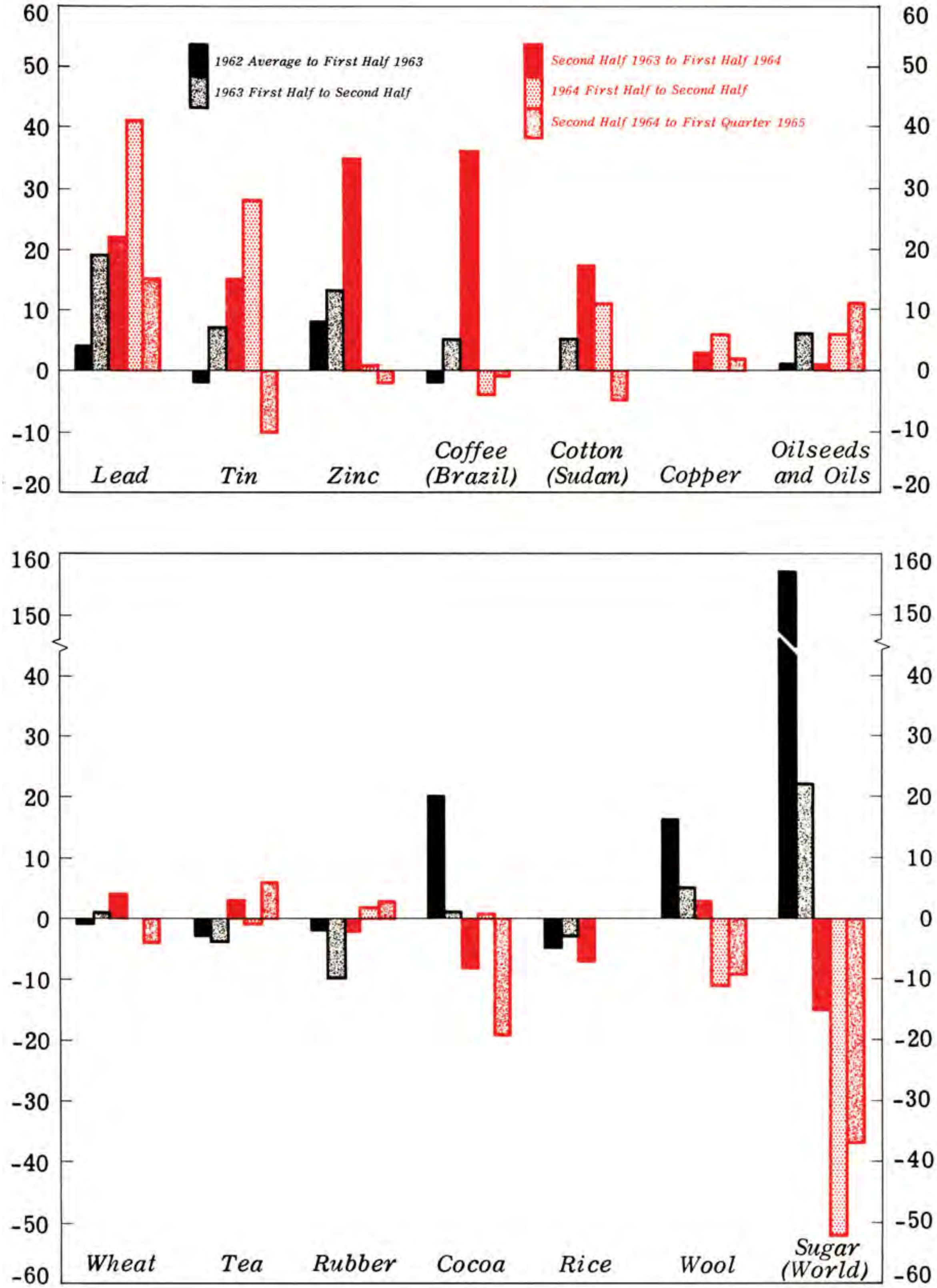
Among individual countries, particularly large gains were made by Canada, Chile, Colombia, Finland, Hong Kong, Morocco, New Zealand, Nigeria, Peru, Saudi Arabia, Spain, and Thailand. In most of these countries, the increases followed relatively large increases in export earnings during 1963. However, for some (e.g., Chile, Peru, Spain, and Thailand) the increases represented a contrast to the small or nominal increases achieved in 1963. For Ceylon and Colombia, the expansion of export earnings in 1964 represented in part a recovery from the contraction suffered in 1963.

During the course of the year, the rate of expansion tended to fall. While the exports of the entire group of countries during the first quarter of 1964 were 16 per cent higher than their exports in the corresponding quarter of 1963, they were only 13 per cent, 8 per cent, and 7 per cent higher in the second, third, and fourth quarters, respectively. This deceleration in the rate of advance was primarily the obverse of a deceleration in imports by the industrial countries (see also Chart 19). It is unlikely that the value of exports of primary products will rise as rapidly during 1965 as it did in the preceding two years.

The continued increase in the exports of the primary product exporting countries induced greater economic activity in these countries in 1964, which in turn resulted in a further expansion in their imports. For most of these countries, the expansion in 1964 was in addition to, and even larger than, the expansion in imports in the

CHART 25. SELECTED PRIMARY PRODUCTS: CHANGES IN AVERAGE PRICES IN 1963 AND 1964

(In per cent)



previous year. Part of this increase was the result of rising export prices in the industrial countries. In the few countries where the 1964 expansion was smaller than that of 1963, it was usually because imports had increased rather sharply in 1963, as in Kuwait and the United Arab Republic. However, imports contracted in a few countries during 1964.

Balance of Payments

The change in the over-all balance of payments position of the primary producing countries from 1963 to 1964 was in large part a reflection of developments in their exports and imports, reviewed in the previous section. The fact that exports continued to rise during 1964 at a substantial, although declining, rate helped to moderate the effect of the rise in imports. Preliminary trade statistics suggest that the aggregate trade deficit of the primary producing countries increased by more than \$0.6 billion from 1963 to 1964, while preliminary balance of payments statistics indicate an increase of some \$1.1 billion in their aggregate deficit on account of goods and services and private transfer payments. This latter increase is apparently attributable in part to higher net payments on account of services. An increase of \$0.6 billion in the inflow on account of economic aid and private capital (including unrecorded transactions) partly offset the deterioration on current transactions, so that the group's aggregate over-all surplus fell from about \$1.6 billion to \$1.1 billion.

As in other recent years, the aggregate balance of payments in 1964 of a limited number of more industrialized countries (Group A of Table 29) differed markedly from that of the other countries (see last line of Table 29). The more industrialized group had an over-all surplus of almost \$900 million, not much lower than in 1963, whereas the aggregate surplus of the less industrialized countries, which had reached \$700 million in 1963, amounted to less than \$300 million in 1964. Even within the latter group, some countries—in particular, certain oil exporting countries—remained in relatively comfortable balance of payments positions, but a number of the less industrialized countries were experiencing increasing strains in their international transactions. Such strains are not always apparent from the statistics, since heavy debt servicing burdens may force countries to restrict deficits or even to run surpluses in other segments of the balance of payments.

More Industrialized Countries

Both exports and imports of the more industrialized group of countries rose rapidly (by 16 per cent and 17 per cent, respectively) between 1963 and 1964. These rates of increase were even higher than those of the manufacturing countries. But since their aggregate imports rose more than exports, there was a substantial rise in their combined deficit on account of goods, services, and private transfers. The increase in the current deficit of the group was for the most part offset by larger net inflows of both long-term and short-term capital, so that the over-all position remained comfortable. Much of the deterioration in the goods and services account was concentrated in Australia and South Africa; all the other countries in the group improved their over-all balance of payments position from 1963 to 1964.

Balance of payments developments in Australia and Canada are reviewed in Chapter 8. Finland's current account deteriorated in 1964, as the increase in imports far exceeded that of exports. There was, however, a large inflow of capital, mainly in the form of bond issues abroad, and the reserves showed a further increase. South Africa's balance of payments changed from surplus to deficit because of a sharp rise in imports, associated mainly with boom conditions in the domestic economy but also influenced by a relaxation of import controls. There was only a modest rise in exports, owing in part to adverse seasonal conditions. The decline in reserves accelerated in the early months of 1965, and during that period the authorities took measures to moderate the domestic expansion of credit, which had been substantial during 1964. Spain increased its surplus from 1963 to 1964 as exports rose sharply because of an exceptionally favorable citrus crop, following a relatively poor one in 1963, and increased exports of manufactured products; net tourist receipts continued to climb rapidly. There was also a substantial inflow of capital, particularly of a

TABLE 28. PRIMARY PRODUCING COUNTRIES: TRADE IN 1963 AND 1964[1]

(Value figures in millions of U.S. dollars)

	Exports f.o.b.				Imports c.i.f.			
			Percentage change				Percentage change	
	1963	1964	1962-63	1963-64	1963	1964	1962-63	1963-64
Countries exporting mainly								
Coffee								
Brazil	1,406	1,433	16	2	1,487	1,263	1	−15
Colombia	446	544	−4	22	506	586	−7	16
Others	1,029	(1,215)	15	18	1,018	(1,235)	12	21
	2,881	3,192	12	11	3,011	3,084	3	2
Other tropical foods								
Ceylon	363	394	−4	9	315	415	−10	32
Nigeria	531	601	7	13	581	712	2	23
Philippines	727	742	31	2	687	868	5	26
Others	1,385	1,565	11	13	1,709	1,911	10	12
	3,006	3,302	12	10	3,292	3,906	5	19
Other agricultural products								
Argentina	1,365	1,410	12	3	981	1,077	−28	10
Australia	2,788	3,040	19	9	2,776	3,315	9	19
New Zealand	910	1,074	14	18	903	961	20	6
Pakistan	417	427	5	2	889	998	20	12
Thailand	466	599	2	28	610	667	9	9
United Arab Republic	522	539	26	3	916	884	20	−3
Others	2,353	2,465	8	5	3,577	3,664	8	2
	8,821	9,554	13	8	10,652	11,566	6	9
Metals and rubber								
Chile	540	623	2	15	520	609	—	17
Indonesia	696	(670)	2	−4	502	(630)	−29	25
Malaya[2]	884	910	3	3	828	818	4	−1
Others	1,108	(1,385)	4	25	1,069	1,346	1	26
	3,228	3,588	3	11	2,919	3,403	−3	17
Petroleum								
Kuwait	1,110	1,218	5	10	324	(330)	12	2
Saudi Arabia	1,050	1,180	7	12	320	(330)	3	3
Venezuela	2,629	2,740	1	4	950	1,155	−15	22
Others	3,760	(4,465)	7	19	2,693	(3,017)	−1	12
	8,549	9,603	5	12	4,287	4,832	−3	13
Other major exporters								
Canada	6,779	8,092	9	19	6,618	7,555	4	14
Finland	1,149	1,291	4	12	1,208	1,505	−2	25
Hong Kong	873	1,012	14	16	1,297	1,496	11	15
India	1,629	1,749	17	7	2,471	2,915	4	18
Mexico	985	1,055	4	7	1,240	1,493	8	20
Morocco	384	434	10	13	447	459	2	3
Peru	540	666	—	23	552	571	4	3
Singapore[2]	1,135	903	2	−20	1,398	1,136	6	−19
South Africa	1,431	1,490	5	4	1,853	2,350	17	27
Spain	736	954	—	30	1,956	2,259	25	15
Yugoslavia	790	892	14	13	1,057	1,321	19	25
	16,431	18,538	8	13	20,097	23,060	8	15
All other countries	4,388	4,785	14	9	7,133	(7,404)	7	4
Grand Total	47,304[3]	52,562[3]	8	11	51,391	57,255	5	11

Source: Based on data from International Monetary Fund, *International Financial Statistics.*
[1] Data in parentheses are partly estimated.
[2] Consolidated data for the trade of Malaysia are not available.
[3] This total differs slightly from that for the two groups of primary producing countries shown in Table 13, owing principally to adjustments for internal transport charges in the figures shown for certain countries in this table.

long-term nature, throughout the year. Since the latter part of 1964, rising internal inflationary pressures have led to a leveling off in the growth of Spain's exports and a rise in imports. There has consequently been a slowing down in the rise of reserves, which at the end of 1964 amounted to more than $1.5 billion.

Less Industrialized Countries

The deterioration from 1963 to 1964 in the balance of payments position of the less industrialized group of countries arose mainly from an increased trade deficit. The deterioration was progressive during 1964, as the rise in exports slowed down while that in imports appeared to be maintained. There was, according to the preliminary figures shown in Table 29, an increase of about $100 million in the net inflow of private capital (including unrecorded transactions) and an increase of about $200 million in official capital and aid. The deterioration in the over-all position was, therefore, somewhat less than the rise in the goods and services deficit.

The collective position of the less industrialized countries in the overseas sterling area changed little, although there was a marked deterioration in the balance of payments of Pakistan, while for India a greatly increased current deficit was offset by heavily expanded foreign aid. The balance of payments of India is reviewed in Chapter 8. The change from surplus to deficit in Pakistan's balance of payments was brought about by a sharp rise in imports (see Table 28) under the impact of a strong monetary expansion in the economy, combined with some liberalization of the import regime. Exports rose only slightly from 1963 to 1964, while apparently foreign aid increased somewhat. The Government of Pakistan has taken steps to limit the increase in bank credit and other measures to curtail the rise in imports; in March it concluded a stand-by arrangement with the Fund for $37.5 million. The deficit in Malaysia's balance of payments was due in part to a further decline in rubber prices, the embargo imposed by Indonesia, and a considerable increase in expenditure for development and, to a lesser extent, for defense. When Malaysia's high reserves are taken into account, the deficit was moderate. Ghana's balance of payments is discussed in Chapter 8.

More than half the Latin American Republics were in over-all surplus in 1963, and again in 1964, although in 1964 their aggregate surplus was slightly reduced. There was a considerable deterioration in the over-all position of Argentina, which in 1963 had been in surplus. (For a discussion of developments in Argentina's balance of payments during 1963, see the Annual Report, 1964, page 96.) Argentina's exports rose slightly beyond the substantial total attained in 1963, and the current account remained in surplus. Reserves declined because of net repayments on foreign debt and remained under pressure because of a heavy debt repayment schedule. The foreign reserves of Argentina are lower than the foreign liabilities of the Central Bank. Exchange controls were introduced in April 1964, and the Argentine peso was progressively devalued from M$N 133 = US$1 at the end of 1963 to M$N 172 = US$1 at the end of May 1965. Developments in Brazil's balance of payments are reviewed in Chapter 8.

Within the last group of countries in Table 29, much of the deterioration in the aggregate balance of payments is accounted for by a reduction in the surplus of Saudi Arabia, whose balance of payments and reserve position nevertheless remained comfortable. Other major changes were an increase in China's surplus—in part influenced by high receipts for sugar during the first half of the year—and shifts from surplus to deficit in both Iran and Iraq. Iran's deficit arose mainly from net capital outflows resulting from net disinvestment by the Petroleum Consortium and net repayments on government loans. Early in 1965, extraordinary receipts of about $185 million in connection with the exploration of new oilfields replenished its reserves. For Iraq, the unfavorable change in the underlying balance of payments was less than the change in the over-all balance. The Iraqi Government had received a loan of $84 million from Kuwait late in 1963, without which its reserves would have risen by only $15 million during that year. In 1964, an increase in government expenditures added to import demand, but this was in part offset by an improvement in the

TABLE 29. PRIMARY PRODUCING COUNTRIES: BALANCE OF PAYMENTS SUMMARIES, 1963 AND 1964[1]

(In millions of U.S. dollars)

	1963					1964				
	Goods, Services, and Private Transfer Payments	Central Govern-ment Capital and Aid	Private Long-Term Capital	Other Short-Term Capital (including commercial banks) and Net Errors and Omissions	Total[2]	Goods, Services, and Private Transfer Payments	Central Govern-ment Capital and Aid	Private Long-Term Capital	Other Short-Term Capital (including commercial banks) and Net Errors and Omissions	Total[2]
A. More Industrialized Primary Producers										
Australia	—83	—87	←660→		490	—331	—119	←515→		65
Canada	—458	—50	561	83	136	—356	—14	624	83	337
Finland	—20	54	59	—57	36	—169	67	119	29	46
New Zealand	—28	8	←—4→		—24	2	—9	←30→		23
Portugal	—21	22	54	—21	34	—20	←130→			110
South Africa	186	24	—150	69	129	—146	63	—87	107	—63
Spain	—244	—21	269	111	115	—42	—13	359	63	367
Total, Group A	—668	—50	1,433	201	916	—1,062	15	1,595	337	885
B. Other Sterling Area										
Burma	19	23	—15	—6	21	—34	20	—	11	—3
Ceylon	—44	25	1	—	—18	—47	52	—	—5	—
Cyprus	—18	—2	8	14	2	1	6	3	—4	6
Ghana	—121	60	31	—5	—35	—84	46	15	—4	—27
Iceland	—5	6	3	—	4	—8	—2	14	3	7
India	—766	842	21	—77	20	—1,172	1,323	28	—154	25
Ireland	—86	10	54	69	47	—99	—6	108	36	39
Jordan	—97	63	4	29	—1	—59	90	4	—23	12
Libya	—21	30	6	11	26	—50	←100→			50
Malaysia	—215	18	124	86	13	—233	←196→			—37
Nigeria	—106	55	48	—32	—35	—219	81	115	59	36
Pakistan	—461	454	77	—29	41	—563	←500→			—63
U.K. Colonial Territories	—112	87	39	14	28	—100	90	40	—	30
Total, Group B	—2,033	1,671	401	74	113	—2,667	2,202	518	22	75
C. Latin American Republics										
Argentina	232	125	—100	—87	170	180	←—230→			—50
Bolivia	—45	36	18	—4	5	—40	←52→			12
Brazil	—218	176	30	—123	—135	88	62	11	6	167
Chile	—185	115	—10	51	—29	—118	←94→		45	21
Colombia	—137	15	129	—81	—74	—148	50	75	34	11
Costa Rica	—30	9	26	—7	—2	—23	14	20	—7	4
Dominican Republic	—47	33	33	—2	17	—58	21	10	14	—13
Ecuador	—8	8	3	8	11	—24	9	6	6	—3
El Salvador	—14	5	20	1	12	—47	←58→			11
Guatemala	—21	16	19	—3	11	—40	1	37	5	3
Haiti	—	2	—2	—3	—3	—9	4	2	1	—2
Honduras	—17	10	9	—2	—	—12	10	8	—2	4
Mexico	—215	85	216	37	123	—393	←438→			45
Nicaragua	—7	3	14	1	11	—13	1	13	7	8
Panama	—38	28	13	3	6	—22	12	3	—12	—19
Paraguay	—9	7	4	—2	—	—8	9	4	—2	3
Peru	—59	50	36	—8	19	7	78	11	—71	25
Uruguay	—5	11	—6	3	3	—9	3	—14	—2	—22
Venezuela	564	—111	—266	—24	163	320	—9	—215	—11	85
Total, Group C	—259	623	186	—242	308	—369	484	181	—6	290
D. Other Countries										
China, Republic of	—1	60	20	—28	51	18	25	13	47	103
Ethiopia	—28	22	12	—6	—	—17	12	11	5	11
Greece	—79	37	94	—37	15	—211	74	124	3	—10
Indonesia	—227	113	10	—20	—124	—140	←—70→			—70
Iran	35	10	—25	—2	18	78	—19	—113	10	—44
Iraq	108	109	—58	—60	99	24	25	—37	—58	—46
Israel	—84	56	134	11	117	—218	87	167	—13	23
Korea	—351	242	42	18	—49	—167	157	10	—2	—2
Morocco	—108	78	2	—22	—50	—27	71	—13	—82	—51
Netherlands Antilles	6	—	—7	—	—1	5	←—5→			—
Philippines	167	1	—30	—83	55	43	55	16	—114	—
Saudi Arabia	158	36	133	—63	264	160	←—89→			71
Somalia	—21	25	—	—1	3	—30	←20→			—10
Sudan	—72	35	4	—3	—36	—90	29	3	9	—49
Syrian Arab Republic	6	—8	—	—8	—10	4	←—14→			—10
Thailand	—110	49	79	34	52	—32	37	63	1	69
Tunisia	—109	52	31	14	—12	—125	95	20	—4	—14
Turkey	—243	187	29	—39	—66	—95	25	45	47	22
United Arab Republic	—278	217	—8	43	—26	—250	←236→			—14
Viet-Nam	—201	220	2	1	22	—233	195	—	—1	—39
Yugoslavia	—89	79	—	—15	—25	—213	←169→			—44
Total, Group D	—1,521	1,620	464	—266	297	—1,516	1,424	291	—303	—104
Grand Total	—4,481	3,864	2,484	—233	1,634	—5,614	4,125	2,585	50	1,146
Grand Total, excluding Group A	*—3,813*	*3,914*	*1,051*	*—434*	*718*	*—4,552*	*4,110*	*990*	*—287*	*261*

For footnotes, see page 77.

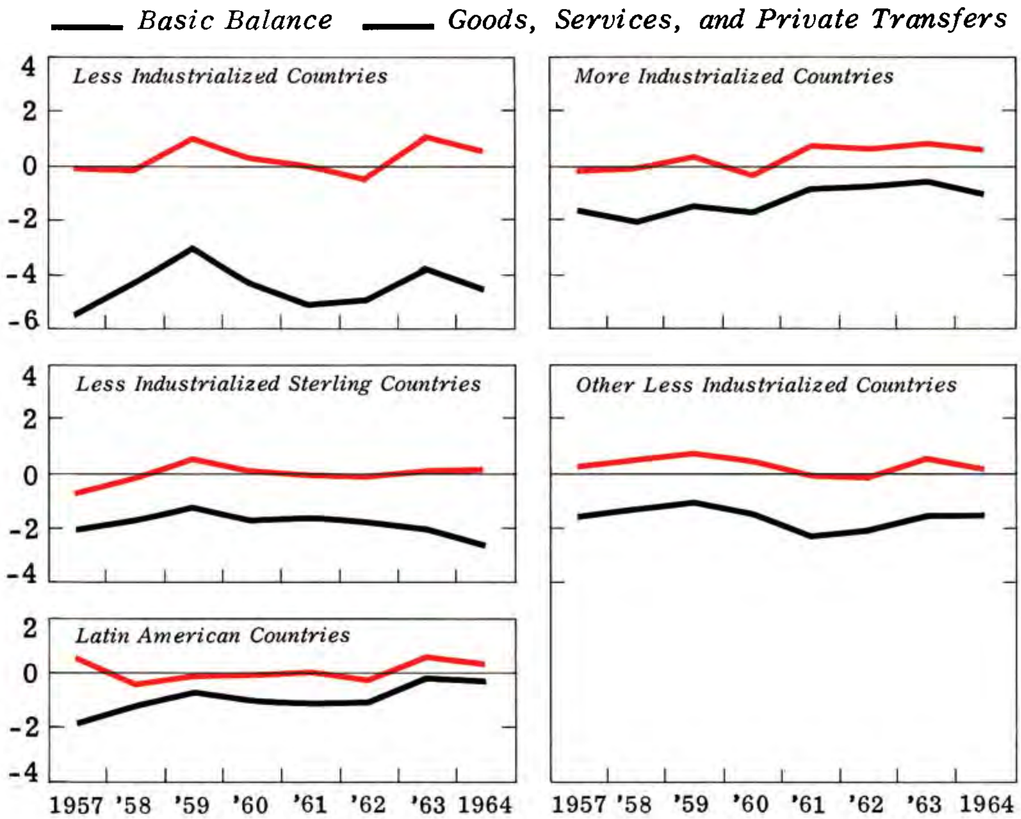
trade accounts owing to a better harvest than in 1963.

* * *

The progress of the primary producing countries as a whole and of certain subgroups over a period of years is illustrated by Chart 26, where balances on account of goods, services, and private transfers are compared with balances on basic account (i.e., current account plus government and private long-term capital). For the two main groups of primary producers, Chart 27 compares the over-all balances (including movements of short-term capital and errors and omissions, in addition to the transactions entering the basic accounts) with the basic balances for the years 1957-64. In each of the last four years, the inflow of capital into the more industrialized primary producing countries has considerably exceeded the current account deficit, resulting in sizable additions to reserves. But although over-all surpluses were achieved in both 1963 and 1964 by the less industrialized countries, between 1957 and the end of 1962 these countries had an over-all surplus in only one year—1959. Chart 27 also shows that, while the movements in the basic and in the over-all balances have in general been similar, there has in each year been an inflow on account of short-term capital and unrecorded transactions

CHART 26. PRIMARY PRODUCING COUNTRIES: BALANCES OF PAYMENTS, 1957-64

(In billions of U.S. dollars)



Footnotes to Table 29.

Source Based on data reported to the International Monetary Fund. For 1964, data for many countries are provisional and in some instances involve estimates by the Fund staff.

[1] No sign indicates credit; minus sign indicates debit.

[2] Represents net official reserve movements, including changes in reserve position in the Fund. No sign indicates an increase in assets, a gold subscription to the Fund, a repayment of a drawing on the Fund, another reduction of Fund holdings, or a reduction of other liabilities; minus sign indicates a decrease in assets, a drawing on the Fund, another increase in Fund holdings, or an increase in other liabilities.

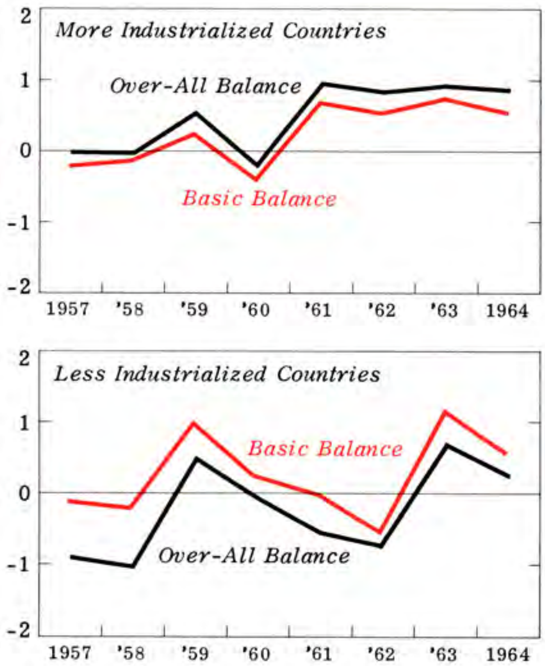
for the more industrialized countries and an outflow from the less industrialized ones.

Domestic Developments

Rising export incomes and increases in foreign reserves permitted the majority of the countries exporting primary products to expand domestic bank credit more rapidly in 1964 than in earlier years. This domestic expansion provided finance for rising imports consistent with increased export receipts and, in most countries, was part of the normal adjustment process. There are grounds for thinking, however, that in some, even though large foreign receipts permitted a rise in domestic credit, this monetary expansion may have gone too far.

CHART 27. PRIMARY PRODUCING COUNTRIES: BASIC AND OVER-ALL BALANCES OF PAYMENTS, 1957-64

(In billions of U.S. dollars)



A number of countries were not able to prevent their international reserves from falling, despite a rise in export earnings. In others, the failure of exports to respond to the high level of world demand can be explained, in part at least, by the pressures of domestic demand encouraged by expansive domestic monetary policies. Relatively easy monetary policies, usually associated with budget deficits, prevailed in a number of countries, including Argentina, Chile, Indonesia, Iran, Mali, Mauritania, Nigeria, and Uruguay; and the financing of government requirements also induced pressures, for example, in Greece and the United Arab Republic. In Brazil, the high level of the budget deficit was reduced during the year.

Among the more important of the developing countries, the domestic situation in India, where there was a sharp rise in prices during 1964, gave ground for special concern. Undoubtedly, a series of bad harvests and the requirements of increased defense expenditures contributed to its difficulties, and gave increased justification for a stand-by arrangement with the Fund, but these adverse circumstances were aggravated by monetary expansion. However, as the rather rapid price increases have been under way for only a relatively short period, it may be less difficult to contain the situation than it is in some other countries where inflation has persisted for some time. It is to be hoped that the corrective measures introduced early in 1965 will prove to be effective in meeting the situation.

A number of other countries took advantage of the rather favorable conditions in 1964 and the early part of 1965 to halt actual or incipient inflations. In Africa, stabilization programs were inaugurated by Burundi, Somalia, and Tunisia. Israel and the Philippines were successful in reducing existing inflationary pressures by limiting the size of government deficits, which made the control of monetary policy easier. But the more severe inflationary situations in Argentina, Brazil, Chile, Indonesia, Korea, and Uruguay persisted. Of these countries, Argentina, Brazil, Chile, and Korea announced plans toward the end of 1964 or early in 1965 to bring their domestic financial situations under control. These plans include measures to restrain increases in wages in order to damp down the wage-price spiral.

Chapter 8

Balances of Payments of Selected Countries

IMPORTANT developments in the balances of payments of several major industrial countries during the past year make it desirable to examine these in more detail. In this chapter an analysis is given of the balances of payments of the United States, Canada, the United Kingdom, the Federal Republic of Germany, France, Italy, and Japan. These are followed by a discussion of the balances of payments of some nonindustrial countries—Australia, Brazil, Ghana, India, and Mexico—to supplement the more general review in Chapter 7.

United States

When considered as a whole, 1964 was in many respects a good year for the balance of payments of the United States. The goods and services surplus was substantially larger than in 1963 and, in spite of an almost equivalent rise in the outflow of U.S. capital, an inflow of foreign short-term capital and other factors helped to keep sales of gold by the United States at a low level. The over-all deficit as measured in Table 25 (p. 67) was about $1 billion lower than in 1963, although on the "regular transactions basis" used by the U.S. Government the improvement was less than $200 million. However, whereas 1963 had been marked by improvement during the year, the U.S. balance of payments deteriorated considerably in the course of 1964 (Table 30). In the last quarter the deficit was large, and in the first quarter of 1965 it continued high, whereas a year earlier the accounts had been approximately in equilibrium. In the first quarter of 1965 the position appeared greatly improved, but so many special factors were involved that conclusions concerning trend were difficult to draw.

The most promising aspect of the U.S. balance of payments in 1964 was the improvement in the goods and services account (including remittances and pensions), the surplus on which rose by $2.6 billion compared with 1963, to a record figure of $7.7 billion. The value of exports rose by 2 per cent more than the growth in U.S. export markets, and continued to exhibit strength through the year. Imports rose considerably less, and altogether the balance of trade accounted for about three fourths of the rise in the goods and services surplus. The remainder of the improvement was derived mainly from investment income, which has been rising considerably in recent years as a result of the large outflow of capital, and from further savings in net military expenditures. Most of the improvement in the goods and services balance from 1963 to 1964 had, however, occurred by the first quarter of 1964; subsequently there was little further advance. While the strong position on this account in 1964 reflected the rather prosperous state of the world economy, the sharp rise in the trade surplus in recent years was apparently in part attributable to the greater stability of prices and costs in the United States than in most of the other industrial countries. An analysis of U.S. trade in particular markets suggests that the competitive position of the United States vis-à-vis these other countries continued to improve from 1963 to 1964 (see Table 21, p. 58).

The rise in the goods and services surplus was offset for the most part by an increase in the outflow of U.S. private capital, which at a little over $6 billion also reached a record level, more than 50 per cent above the 1963 figure. About two thirds of the rise took the form of short-term capital, but the outflow of long-term bank loans and direct investment also rose substantially. New foreign issues fell slightly from 1963 to 1964 under the influence of the Interest Equalization Tax. The effect of this Tax had been felt immediately after it was proposed in July 1963, although not all the subsequent decline in new issues may be attributable to it. Its enactment in September 1964 removed uncertainty as to the transactions that would be covered, and was followed by a temporary upsurge in new issues,

TABLE 30. UNITED STATES: BALANCE OF PAYMENTS SUMMARY, 1963–FIRST QUARTER 1965[1]

(In millions of U.S. dollars)

			1964				1965
	1963	1964	First quarter	Second quarter	Third quarter	Fourth quarter	First quarter[2]
A. Goods, Services, Aid, and Long-Term Capital							
Main categories, seasonally adjusted, excluding advance debt repayments							
Exports financed by government grants and capital	2,793	2,812	671	683	742	716	615
Other exports f.o.b.	19,276	22,476	5,478	5,384	5,640	5,974	4,974
Imports f.o.b.	—16,992	—18,619	—4,410	—4,599	—4,709	—4,901	—4,663
Trade surplus	5,077	6,669	1,739	1,468	1,673	1,789	926
Net military expenditures	—2,270	—2,062	—538	—529	—523	—472	—485
Investment income	3,383	4,053	1,055	1,050	1,045	903	1,180
Other services, remittances, and pensions	—1,110	—939	—259	—262	—203	—215	—293
Total goods, services, remittances, and pensions	5,080	7,721	1,997	1,727	1,992	2,005	1,328
Government grants and capital	—3,907	—3,685	—805	—923	—925	—1,032	—796
Private long-term capital	—3,345	—4,241	—732	—702	—1,235	—1,572	—1,442
U.S. direct investment abroad	*—1,976*	*—2,376*	*—464*	*—540*	*—551*	*—821*	*—1,003*
New foreign security issues	*—1,250*	*—1,063*	*—124*	*—183*	*—157*	*—599*	*—299*
Transactions in outstanding foreign securities	*—49*	*193*	*94*	*40*	*35*	*24*	*51*
Redemptions and other U.S. long-term capital	*—396*	*—1,105*	*—244*	*—113*	*—490*	*—258*	*—436*
Foreign long-term capital	*326*	*110*	*6*	*94*	*—72*	*82*	*245*
Total	—2,172	—205	460	102	—168	—599	—910
Seasonal influences	—	—	304	—88	—568	352	339
Advance debt repayments	326	122	52	33	30	7	10
Total	—1,846	—83	816	47	—706	—240	—561
B. Unrecorded Transactions	—401	—1,161	—72	—40	—352	—697	126
C. Short-Term Capital, n.i.e.							
U.S. private assets	—785	—2,111	—625	—597	—202	—687	249
Prepayments for military equipment	334	222	163	—62	—28	149	55
Other foreign nonliquid capital	71	371	—3	28	269	77	—20
Foreign liquid capital	157	114	—51	32	—18	151	2
Total	—223	—1,404	—516	—599	21	—310	286
D. Liquid Liabilities to Foreign Commercial Banks	462	1,440	278	82	580	500	168
E. Total (B through D)	—162	—1,125	—310	—557	249	—507	580
F. Reserves and Related Items							
IMF position	30	266	131	118	135	—118	68
Liquid liabilities to central banks and governments[3]	1,630	1,037	—455	207	387	898	—861
U.S. convertible currency holdings (increase —)	—113	—220	—228	258	—45	—205	—58
Gold sales (purchases —)	461	125	46	—73	—20	172	832
Total	2,008	1,208	—506	510	457	747	—19
Memorandum item: reduction in monetary reserve assets and increase in liquid liabilities, seasonally adjusted[4]	2,670	2,798	257	582	593	1,366	668

Source: U.S. Department of Commerce, *Survey of Current Business*, June 1965.

[1] No sign indicates credit; minus sign indicates debit.

[2] Preliminary.

[3] Changes in foreign official holdings of U.S. Government nonmarketable, medium-term, inconvertible securities (credit of $63 million for the first quarter of 1963 and debit of $10 million for the second quarter, $95 million for the third quarter and $1 million for the fourth quarter of 1963, $55 million for the first quarter, $8 million for the second quarter, $2 million for the third quarter, and credit of $29 million for the fourth quarter of 1964) are included with liquid liabilities.

[4] Excluding the U.S. Government securities referred to in footnote 3.

mainly of Canadian securities, for which an expected exemption had been granted. Transactions in outstanding foreign issues, for which no exemptions from the tax had been proposed, changed from a small outflow in 1963 to a somewhat larger inflow in 1964.

The rise in the outflow of U.S. capital is difficult to explain fully, although some of the underlying factors can readily be seen. A major influence appears to have been the divergence in economic policies between the United States and a number of other industrial countries. In the United States, economic policies continued to be directed broadly toward supporting expansion, with some shift in emphasis toward reliance on fiscal rather than monetary instruments. In a number of the other industrial countries, fiscal and, even more, monetary policies were made more restrictive—either on balance of payments considerations, or to contain upward pressures on wages and prices, or for both reasons. This divergence influenced both interest rates and credit availabilities in various markets and may well explain much of the increase in U.S. external bank loans on both long term and short term. It may even have stimulated direct investment, in that some companies in countries with restrictive monetary policies appear to have been induced by these policies to invite participation by U.S. or other foreign organizations. Another factor stimulating a rise in the outflow of direct investment capital from the United States was the evident progress made during the year toward economic integration in the European Economic Community. The rise in the outflow of such capital occurred in spite of indications that U.S. profit rates were rising in relation to those in most other industrial countries, particularly those in the EEC.

From 1963 to 1964 there was a reduction in the inflow of foreign private long-term capital into the United States but a sharp rise in that of short-term capital—in particular, liquid funds of foreign commercial banks. As a result, the deficit settled through movements in U.S. reserves and in other countries' reserves in the United States fell considerably. This helped to keep the net outflow of gold at a low level. Other factors having the same tendency were net sales of gold by Italy, which reduced its gold holdings in spite of a considerable increase in its total reserves, and by the United Kingdom.

It is difficult to express the over-all balance of payments position of the United States in a single figure, and for 1964 estimates of the deficit vary widely, depending on the conceptual basis adopted; this differs mainly in the role assigned to movements of foreign liquid funds other than exchange reserves. In official U.S. statistics such movements are counted as financing a deficit (whereas changes in U.S. liquid funds abroad other than reserves are included in the deficit itself, "above the line"). Other methods of measurement, including that customarily used in the Fund's analysis of world payments problems, treat the two symmetrically as part of the over-all deficit "above the line." As the net inflow of foreign nonofficial liquid funds was very large in 1964, the official estimates of the U.S. deficit during that year show much larger amounts than those in Table 25, and indeed show little change from 1963 to 1964. Both series, however, show a considerable worsening of the balance of payments after the first quarter of 1964.

Several factors toward the end of 1964 and early in 1965 added to the pressures on the U.S. dollar. Among these were a dock strike, postponed from October, which finally broke out in January and brought about a considerable deterioration in the trade balance until it ended on February 20; the announcement by the French Government of plans for reducing its dollar holdings by purchasing gold; the expectation that the U.S. Government would soon take additional action to stem the outflow of capital; and the psychological effects of the announcement of very high figures for the U.S. deficit at a time when the international monetary system was under pressure stemming from the most serious sterling crisis since 1947.

On February 10, the President of the United States announced a new program for dealing with the balance of payments problem, mainly addressed to the outflow of capital. This program included invoking statutory authority to apply the Interest Equalization Tax to bank loans with maturities of one year or more, a two-year extension of the tax to December 1967, and a broadening of it to cover nonbank credit granted for periods of one to three years. A voluntary program was also announced under which financial institutions were requested to limit the increase in their foreign credits so that by March 1966, at the latest, they would not be more than 5 per cent in excess of their December 1964 levels. The ceiling of 5 per cent for expansion of lendings by financial institutions other than banks was to apply only to loans and investments with maturities of up to ten years. Within these over-all limits, absolute priority was to be given to export financing; special care was to be exercised to avoid possible adverse effects on Canada, Japan, and the United Kingdom, and credits to less developed countries were to be given high priority. It has been estimated that this program will lead to a reduction of capital exports reported by banks from $2.5 billion in 1964 to less than $1 billion in 1965. Industrial concerns have been asked to take steps to improve their individual balances of payments—by expanding exports and other receipts from abroad, by transferring income receipts from developed countries other than Canada, and by limiting outflows of capital to developed countries other than Canada; they are to report on their results to the Secretary of

Commerce. It is noteworthy that these programs involve no reductions in current payments for goods and services.

Canada

The continued upswing in the Canadian economy during 1964 was accompanied by a further improvement in the balance of payments (Table 31). After a comparatively unfavorable first quarter, the balance of payments on current and capital accounts combined strengthened considerably and progressively during the remainder of the year. Canada added $337 million to its foreign exchange reserves, mostly in the form of an improvement by $257 million in its position in the Fund.

The current account deficit for the full year was the lowest in a decade, owing in part to extraordinary levels of wheat exports. Total exports rose to the impressive extent of 16 per cent, and although large shipments of wheat under bulk sales contracts with the U.S.S.R. and other foreign governments were predominant in the growth of exports, a wide range of manufactured goods, as well as the traditional Canadian metals, minerals, and forest products, were also exported in greatly expanded quantities. At the same time imports rose by 15 per cent; a particularly large increase in imports of machinery and equipment was associated with a rapid rise in business investment in plant and equipment. In the fourth quarter of 1964 and the first quarter of 1965 the current account deficit recurred as wheat shipments declined to more normal levels.

The inflow of long-term capital was abnormally low during the first three quarters of the year, but increased very sharply in the fourth quarter after the enactment of the U.S. Interest Equalization Tax and the granting of the exemption for new issues of Canadian securities. Short-term funds, on the other hand, moved outward after

TABLE 31. CANADA: BALANCE OF PAYMENTS SUMMARY, 1963–FIRST QUARTER 1965[1]

(In millions of U.S. dollars)

			1964[2]				1965[2]
	1963	1964[2]	First quarter	Second quarter	Third quarter	Fourth quarter	First quarter
A. Goods, Services, and Transfer Payments							
Exports	6,551	7,620	1,600	2,032	2,019	1,969	1,688
Imports	—6,086	—6,973	—1,570	—1,894	—1,690	—1,819	—1,740
Trade balance	465	647	30	138	329	150	—52
Nonmonetary gold	142	133	31	38	32	32	32
Transportation	—75	—56	—5	—19	—18	—14	—8
Travel	19	—48	—89	—45	111	—25	—108
Investment income	—598	—623	—160	—143	—143	—177	—144
Other services	—381	—386	—105	—93	—90	—98	—78
Transfer payments	—87	—86	—19	—19	—23	—25	—19
Total	—515	—419	—317	—143	198	—157	—377
B. Long-Term Capital							
Direct investment in Canada	222	153	46	9	28	70	56
Canadian direct investment abroad	—102	—83	—37	—42	—	—4	—32
Transactions in Canadian securities							
Special issues sold to U.S. insurance companies	116	—	—	—	—	—	—
Other new issues	780	974	131	290	92	461	229
Other transactions and retirements	—430	—349	—138	—83	—24	—104	—137
Transactions in foreign securities	21	—53	—6	—33	—5	—9	—31
Columbia River Treaty (net)	—	50	—	—	50	—	—
Other loans by Canadian Government (net)	6	—	2	2	1	—6	5
Other	—46	4	—32	—37	58	15	48
Total	567	695	—34	106	200	423	138
C. Total (A plus B)	52	276	—351	—37	398	266	—239
D. Private Short-Term Capital (including net errors and omissions)	84	61	313	100	—253	—99	173
E. Monetary Movements							
IMF position	—80	—257	—79	—6	—55	—117	—43
Official gold and foreign exchange (increase —)	—56	—80	117	—57	—90	—50	109
Total	—136	—337	38	—63	—145	—167	66

Source: Based on data published by the Dominion Bureau of Statistics.
[1] No sign indicates credit; minus sign indicates debit.
[2] Preliminary.

midyear, following heavy inflows in the first six months. Over all, the capital inflow for the year was about $100 million larger than in 1963. An unusual feature of capital flows during the year was the receipt and disposition of $254 million raised for the Columbia River Project; all but $50 million of this sum was invested in special medium-term nonmarketable U.S. Government securities maturing serially over a seven-year period, which will be added to the official Canadian exchange reserves as the receipts mature.

United Kingdom

In the course of 1963 the balance of payments of the United Kingdom on current account had been deteriorating, under the impact of a considerable rise in imports associated with the upswing in economic activity. In the first quarter of 1964, the seasonally adjusted current account balance swung into deficit after having been close to equilibrium during the second half of 1963. It remained in deficit throughout 1964 (Table 32). At the same time the outflow of long-term

TABLE 32. UNITED KINGDOM: BALANCE OF PAYMENTS SUMMARY, 1963–FIRST QUARTER 1965[1]

(In millions of U.S. dollars)

			1964[2]				1965[2]
	1963	1964[2]	First quarter	Second quarter	Third quarter	Fourth quarter	First quarter
A. Goods, Services, and Transfer Payments							
Exports f.o.b., seasonally adjusted	12,004	12,519	3,103	3,116	3,108	3,192	3,262
Imports f.o.b., seasonally adjusted	−12,228	−14,067	−3,455	−3,517	−3,547	−3,548	−3,371
Trade balance, seasonally adjusted	−224	−1,548	−352	−401	−439	−356	−109
Services and transfer payments, seasonally adjusted	493	501	137	115	131	118	126
Total, seasonally adjusted	269	−1,047	−215	−286	−308	−238	17
Seasonal influences	—	—	64	118	−202	20	−37
Total, unadjusted	269	−1,047	−151	−168	−510	−218	−20
B. Long-Term Capital Movements, n.i.e.							
Official long-term	−294	−336	−78	−56	−79	−123	−39
Private long-term							
Investment abroad (net)	−946	−1,184	−291	−316	−280	−297	−330
Investment in U.K. (net)	753	481	128	53	166	134	117
Total	−487	−1,039	−241	−319	−193	−286	−252
C. Total (A plus B)	−218	−2,086	−392	−487	−703	−504	−272
Memorandum item: loan service, due to U.S. and Canada, but not paid	—	*−174*	—	—	—	*−174*	—
Total (A plus B including loan service)	*−218*	*−2,260*	*−392*	*−487*	*−703*	*−678*	*−272*
D. Errors and Omissions	−205	2	126	47	31	−202	−87
E. Short-Term Capital Movements, n.i.e.							
Miscellaneous capital	−109	154	31	98	−6	31	−14
Foreign currency liabilities (net) of banks	−48	386	98	154	101	33	412
Sterling liabilities (net) other than Group F							
Sterling area countries	93	−185	28	−31	81	−263	−17
Other	8	−142	−101	168	174	−383	−154
Total	−56	213	56	389	350	−582	227
F. Official Monetary Movements							
IMF position	13	1,005	—	−2	2	1,005	−17
Central bank assistance	—	605	—	15	185	405	414
Sterling liabilities (net) to overseas central monetary institutions							
Sterling area countries	384	61	115	232	−59	−227	−218
Other countries	−66	−141	98	−149	29	−119	−33
U.K. gold and currency reserves (increase —)							
Gold	98	348	25	20	137	166	25
Foreign currencies	50	−7	−28	−65	28	58	−39
Total	479	1,871	210	51	322	1,288	132
Memorandum item: waiver of loan service, due to U.S. and Canada	—	*174*	—	—	—	*174*	—
Total (Group F) including waiver	*479*	*2,045*	*210*	*51*	*322*	*1,462*	*132*

Source: Central Statistical Office, *Economic Trends*.
[1] No sign indicates credit; minus sign indicates debit.
[2] Preliminary.

capital was much higher than usual, and a very substantial deficit on current and long-term capital account was incurred during the year, compared with a near balance during the three preceding years.

Early in 1964 the U.K. authorities attempted to moderate the rate of increase in domestic expenditure, which had been rising faster than productive capacity in 1963. Nevertheless, total expenditure continued to outstrip production and the volume of imports was appreciably higher than in 1963; import prices were, on average, also much higher. Almost all available labor was employed, and there is evidence of some spillover of demand into imports during the year. The export performance was also disappointing, as has been the long-term trend in U.K. exports for many years. The failure of U.K. exports to rise at an adequate rate has been a major obstacle to reconciling the policy objectives of achieving a satisfactory rate of economic growth and of maintaining balance of payments equilibrium.

In the first half of 1964 the basic deficit was not reflected in a decrease of gold and convertible currency holdings because there was a further large growth in the balances of the overseas sterling area (OSA) and an inflow of short-term capital. In the third quarter, the inflow of short-term capital continued, but OSA balances rose only slightly and the United Kingdom drew on some assistance from foreign central banks as well as on its own reserves. In the fourth quarter, there was a considerable withdrawal of short-term funds; leads and lags were also unfavorable to the United Kingdom. For the year as a whole, the United Kingdom relied on external assistance amounting to $1,605 million, of which the drawing on the Fund, under a stand-by arrangement concluded in August 1964, represented $1,000 million. In addition, relief was provided through a deferment of the debt service due on U.S. and Canadian postwar loans. Nevertheless, the United Kingdom's gold and foreign exchange reserves fell by $341 million, to $2,316 million on December 31. The total financing through the use of reserves and external assistance was a little less than the deficit on current and long-term capital account; short-term capital movements and changes in sterling reserves did not on the whole add to the balance of payments problems during 1964.

The new Government which took office in the middle of October quickly introduced a series of measures to help to correct the external imbalance. As a temporary measure, a charge of 15 per cent was levied on about one third of total imports; an export rebate was introduced; and duties on oil and petroleum were raised. The bank rate was raised from 5 per cent to 7 per cent late in November, and credit facilities totaling $3 billion were negotiated with foreign central banks.

In the early months of 1965, the current account of the balance of payments appeared, on a seasonally adjusted basis, to move into approximate equilibrium, although part of this improvement was probably caused by some imports being delayed by the U.S. dock strike; exports in the first quarter were about 5 per cent higher in value than in the same period of 1964, while imports fell. There were further outflows of funds from London at times in January and again before the April budget; during this period heavy recourse was again had to central bank assistance. A further drawing on the Fund in May for $1,400 million was, for the most part, used to repay central banks.

The budget statement on April 6 stressed that the first priority of economic policy was the correction of the balance of payments position. The budget provisions (discussed in Chapter 5) were designed to control the growth of domestic demand, and, by the use of exchange control and a reorganization of the corporate tax structure, to reduce the outflow of long-term capital by about $300 million a year, in addition to the fall from the exceptionally high rate in 1964 that could in any case be expected. The Chancellor of the Exchequer said that his aim was a basic equilibrium (i.e., on the combined current and long-term capital accounts plus allowance for the relevant portion of the balancing item) by the end of 1966. He intended to get most of the way toward closing the gap in 1965 and to complete the process in the course of 1966. He recognized the need to reduce further the import charge and to abolish it as the external position improved. The charge was cut to 10 per cent on April 27.

The prime objective of monetary policy at the moment is also to help to correct the external imbalance. Interest rates have remained high, and bank credit, following the rapid increase in 1964, tended to decline in the early months of 1965. In his budget speech, the Chancellor said that further measures to reinforce control over bank lending would be taken if it proved necessary; the subsequent call for special deposits and later changes in policy are noted in Chapter 5. The introduction of the budget and the related policy measures had a favorable effect on confidence in sterling.

The Government has also been taking a variety of long-term measures to strengthen competitiveness and thus to help the balance of payments. An incomes policy has been introduced; the main principles and the machinery for the implementation of this policy have been agreed at all stages with the representatives of the Trades Unions and the employers. Earlier attempts to evolve an incomes policy lacked such a broad agreement. A drive for the modernization and technical improvement of industry has also been initiated. This involves the establishment of a number of councils for particular industries to suggest specific methods of improving efficiency.

Federal Republic of Germany

One of the most helpful developments in international transactions during the past year was the return of the balance of payments of Germany to approximate equilibrium, from a strong surplus position at the beginning of the year (Table 33). During the greater part of 1963 the German balance of payments had been in surplus. Initially the source of the surplus was an inflow of capital, largely representing purchases of long-term government securities yielding high rates of interest. Toward the end of the year, however, this was supported by a sharp rise in the surplus on goods and services account, attributable for the most part to the rising inflationary pressures in the other EEC countries, mainly Italy and France. The near elimination of the over-all surplus in the course of 1964 was aided by action by the German authorities to discourage an inflow of capital. It also resulted in part from a reduction in the goods and services surplus, which may be ascribed partly to measures taken by the other EEC countries to restrain inflationary pressures and partly to the increase in import demand associated with a remarkable rise in economic activity in Germany. The balance of payments remained in approximate equilibrium in the first quarter of 1965.

The measures to discourage an inflow of capital included the withholding tax on foreigners' income from German securities discussed in Chapter 5. An outflow was also indirectly encouraged by the U.S. Interest Equalization Tax, which made international borrowers interested in finding new markets for their issues. Altogether, movements of long-term capital (including government as well as private capital) changed from a net inflow of about $530 million in 1963 to a net outflow of about $230 million in 1964. The net effect of this change on the balance of payments, however, was to a considerable extent offset by opposite changes in the flows of private short-term capital (other than changes in the net liquid position of the commercial banks, but including unrecorded transactions), even though the efforts of the German authorities to discourage an inflow of foreign short-term funds continued.

France

Like the German balance of payments, that of France moved nearer to equilibrium between 1963 and 1964. However, in France the progress toward equilibrium was rather modest and it was interrupted early in 1964. After the first quarter of the year the tendency appeared to be again toward a larger surplus (Table 34).

The official French balance of payments statistics cover transactions of metropolitan France and the rest of the French franc area with the non-franc area. Between 1963 and 1964 the current account surplus of metropolitan France with the non-franc area fell from a little over $500 million to a little less than $100 million. There was a net inflow of private long-term capital from the non-franc area into metropolitan France in both years of well over $500 million. The surplus of metropolitan France on account of current and private long-term capital transactions with the non-franc area was thus reduced by about $400 million. At the same time, the surplus of the

TABLE 33. FEDERAL REPUBLIC OF GERMANY: BALANCE OF PAYMENTS SUMMARY, 1963–FIRST QUARTER 1965[1]

(In millions of U.S. dollars)

			1964[2]				1965[2]
	1963	1964[2]	First quarter	Second quarter	Third quarter	Fourth quarter	First quarter
A. Goods, Services, and Transfer Payments							
Exports f.o.b.	14,566	16,219	3,888	4,052	3,866	4,413	4,343
Imports c.i.f.	—12,994	—14,618	—3,272	—3,542	—3,672	—4,132	—4,038
Other merchandise	—103	—181	—55	—22	—52	—52	—42
Trade balance	1,469	1,420	561	488	142	229	263
Paid services to foreign troops	1,072	1,055	251	255	260	289	—4
Other services	—1,082	—1,169	—235	—272	—370	—292	
Total goods and services	1,459	1,306	577	471	32	226	259
Transfer payments	—1,239	—1,205	—281	—353	—291	—280	—306
Total	220	101	296	118	—259	—54	—47
B. Long-Term Capital							
Bonds	443	—122	63	—194	7	2	—88
Shares	153	12	14	—49	40	7	—52
Other private long-term capital	188	154	36	40	—9	87	222
Other government long-term capital	—295	—314	—66	—62	—66	—120	—47
Repayments on post-EPU claims	36	35	3	3	25	4	1
Other Bundesbank assets (increase —)[3]	5	7	2	2	2	1	2
Total	530	—228	52	—260	—1	—19	38
C. Total (A plus B)	750	—127	348	—142	—260	—73	—9
Total, excluding certain extraordinary transaction[4]	*709*	*—169*	*343*	*—147*	*—287*	*—78*	*—12*
D. Short-Term Capital, n.i.e. (including net errors and omissions)							
Government	—79	—176	—95	4	19	—104	21
Commercial bank credits (net)	32	39	—154	—29	90	132	—266
Other	6	43	166	14	—74	—63	45
Net errors and omissions	—132	471	235	107	190	—61	302
Total	—173	377	152	96	225	—96	102
E. Commercial Bank Liquid Capital (net)							
Foreign exchange (increase —)	—72	—118	—235	72	—41	86	—177
Foreigners' deposits	215	91	—167	63	—5	200	—73
Total	143	—27	—402	135	—46	286	—250
F. IMF Position and Net Reserves							
IMF position	—35	—360	—92	—55	1	—214	32
Bundesbank liabilities	—29	4	8	9	—21	8	16
Foreign exchange (increase —)[5]	—491	538	96	85	168	189	104
Monetary gold (increase —)	—165	—405	—110	—128	—67	—100	5
Total	—720	—223	—98	—89	81	—117	157

Source: Deutsche Bundesbank, *Monthly Report,* May 1965.
[1] No sign indicates credit; minus sign indicates debit.
[2] Preliminary.
[3] Covers IBRD bonds and notes and repayments received on consolidated credits and other Bundesbank assets of limited usability.
[4] This balance is intended to facilitate analysis of the more basic factors in the balance of payments. It excludes the following extraordinary transactions: (a) advance debt redemption (none in period covered), (b) repayments on post-EPU claims, and (c) other Bundesbank assets, i.e., IBRD bonds and notes, repayments received on consolidated credits, and other Bundesbank assets of limited usability. However, it includes private transactions in securities, which are likely to fluctuate widely in the short run. Such transactions should be taken into account in evaluating the balance. These figures do not agree with the basic balances shown in Table 23 because of certain conceptual differences; for instance, transactions in German securities are classified by the sector of domestic creditor or debtor in Table 23, whereas, in this table, they are classified according to the sector of domestic transactor.
[5] Covers freely usable foreign exchange and earmarked assets.

overseas franc area with the non-franc area rose by $130 million. In 1963, the French Government made advance repayments on foreign debt amounting to $280 million. No similar payments were made in 1964, and the increase in French net reserves over the year fell only slightly, from $856 million in 1963 to $815 million in 1964.

Toward the end of 1963 the current surplus of metropolitan France with the non-franc area was being sharply reduced under the influence of strong pressures of domestic demand, and in the first quarter of 1964 there was a small current deficit with the non-franc area, while the over-all balance of payments of the franc area as a whole was approaching equilibrium. However, a current surplus vis-à-vis the non-franc area was re-established in the second quarter and maintained during the remainder of the year. The restoration of the surplus position on current account may be associated with the measures taken by the French Government to restrain inflationary pressures, which brought the rise in

TABLE 34. FRANCE: BALANCE OF PAYMENTS SUMMARY, 1963 AND 1964[1]

(In millions of U.S. dollars)

	1963	1964[2,3]	1964[2] First quarter	Second quarter	Third quarter	Fourth quarter
A. Goods, Services, and Transfer Payments						
Exports f.o.b.	6,745	7,587	1,825	1,833	1,830	1,935
Imports f.o.b.	−6,568	−7,700	−1,950	−1,888	−1,752	−2,011
Trade balance	177	−113	−125	−55	78	−76
Services	245	136	33	77	−65	51
Transfer payments	89	64	−1	17	19	27
Total	511	87	−93	39	32	2
B. Private Long-Term Capital						
Foreign direct investment in France	212	308	49	61	80	98
Other foreign capital	245	242	61	64	52	49
French direct investment abroad	−94	−126	−15	−29	−24	−23
Other French capital	153	124	15	47	24	23
Total	516	548	110	143	132	147
C. Official Long-Term Capital						
Advance debt redemption	−281	—	—	—	—	—
Other official	−148	−82	−13	−11	−42	−17
Total	−429	−82	−13	−11	−42	−17
D. Total (A through C)	598	553	4	171	122	132
Total, excluding advance debt redemption	*879*	*553*	*4*	*171*	*122*	*132*
E. Private Short-Term Nonmonetary Capital	−72	−100	−27	−23	−27	−24
F. Total (D plus E)	526	453	−23	148	95	108
G. Net Transactions of Overseas Franc Area	132	260	66	50	53	76
H. Net Errors and Omissions						
Operations pending settlements	−48	62	42	24	−12	8
Other net errors and omissions	44	2	18	47	39	38
Total	−4	64	60	71	27	46
I. Commercial Bank Short-Term Capital[4]						
Liabilities	391	269	−48	132	−121	306
Assets (increase —)	−189	−231	37	−64	43	−247
Total	202	38	−11	68	−78	59
J. Official Monetary Movements						
IMF position (increase —)	−12	−168	−51	−45	32	−104
Other liabilities	−39	—	−11	−7	−19	37
Foreign exchange (increase —)	−217	−92	93	−132	4	−57
Monetary gold (increase —)	−588	−555	−123	−153	−114	−165
Total	−856	−815	−92	−337	−97	−289

Source: Data provided by the French authorities.

[1] Groups A through F cover settlements of metropolitan France with the non-franc area. Groups I and J cover changes in assets and liabilities of institutions in metropolitan France arising from transactions of both parts of the franc area with the rest of the world. No sign indicates credit; minus sign indicates debit.

[2] Preliminary.

[3] Quarterly figures do not add to annual data since certain adjustments made for the year cannot be distributed between the quarters.

[4] Commercial bank long-term capital is included in private long-term capital (Group B).

economic activity to a virtual halt in the course of 1964.

The increase in the surplus of the overseas franc area with the non-franc area was due in part to the generally higher level of prices for primary products in 1964 than in 1963, and to that extent may be a temporary phenomenon. However, the surplus which the overseas franc area can realize in its transactions with the non-franc area depends to a considerable extent on the pattern of its transactions with metropolitan France, on which complete statistical information is not available. Usually the overseas franc area has had a deficit with France on account of trade and commercial services, which has been more than offset by expenditures by the French Government, including military expenditures and economic aid. Private French investment in the overseas franc area has in recent years presumably been rather smaller than the rather sizable inflow of capital into France from that area, which has been largely associated with the repatriation of French settlers.

It is the aim of the French authorities that the balance of payments of metropolitan France should show a net outflow of private capital and economic aid extended, offset by a surplus on goods and services account. Although the available statistics do not permit an accurate appraisal of France's balance of payments with the world, it is apparent that it attained a substantial over-all surplus in 1964, as in a number of other recent years. The French Government has expressed a desire to see a reduction in the inflow of foreign capital from the non-franc area; a reduction in the over-all surplus could also be achieved through action to encourage an outflow of capital to that area. Some reduction in the surplus, through adjustment of the current account, might result from steps taken by the French authorities to stimulate domestic investment. However, in the early months of 1965 the large French over-all surplus still persisted, while the French authorities accelerated their gold purchases from the United States. It is understood that they intend to reduce their holdings of foreign exchange, which totaled some $1.4 billion at the end of 1964, and to convert current accruals of foreign exchange into gold.

Italy

The balance of payments of Italy made a dramatic recovery during 1964 (Table 35). At the

TABLE 35. ITALY: BALANCE OF PAYMENTS SUMMARY, 1963 AND 1964[1]

(In millions of U.S. dollars)

			1964[2]			
	1963	1964[2]	First quarter	Second quarter	Third quarter	Fourth quarter
A. Goods, Services, and Transfer Payments						
Exports f.o.b.	4,969	5,875	1,301	1,440	1,531	1,603
Imports f.o.b.	—6,777	—6,455	—1,853	—1,703	—1,352	—1,547
Trade balance	—1,808	—580	—552	—263	179	56
Transportation and merchandise insurance	—172	—195	—69	—38	—4	—84
Travel	749	825	90	183	352	200
Investment income	—114	—95	—22	—45	—25	—3
Workers' earnings	299	325	58	83	98	86
Other services	99	105	—3	32	17	59
Private transfer payments	321	300	65	76	86	73
Central government transfer payments	—31	—25	—7	—7	—2	—9
Total, unadjusted	—657	660	—440	21	701	378
Total, seasonally adjusted	—657	660	—230	127	455	308
Exports f.o.b.	*4,969*	*5,875*	*1,318*	*1,471*	*1,537*	*1,549*
Imports f.o.b.	*—6,777*	*—6,455*	*—1,793*	*—1,668*	*—1,400*	*—1,594*
Travel	*749*	*825*	*172*	*192*	*204*	*257*
Other services and transfer payments	*402*	*415*	*73*	*132*	*114*	*96*
B. Capital Movements (excluding Groups D and E) and Net Errors and Omissions						
Remittances of Italian banknotes[3]	—1,477	—577	—262	—142	—113	—60
Foreign investments in Italy[3]	1,293	1,088	246	430	199	213
Italian investments abroad	—102	—109	—29	—13	—44	—23
Central government capital	—33	14	15	—52	25	26
Other and net errors and omissions	—276	—299	35	—18	—266	—50
Total	—595	117	5	205	—199	106
C. Total (A plus B)	—1,252	777	—435	226	502	484
D. Commercial Banks' Capital						
Liabilities	476	—287	—240	—149	—140	242
Assets (increase —)	174	—155	43	2	35	—235
Total	650	—442	—197	—147	—105	7
E. Official Monetary Movements						
IMF position	—23	79	225	—	—124	—22
Monetary gold (increase —)	—100	237	200	—4	44	—3
Other foreign assets of UIC and Bank of Italy (increase —)	725	—651	207	—75	—317	—466
Total	602	—335	632	—79	—397	—491

Source: Ufficio Italiano dei Cambi (UIC), *Movimento Valutario,* and Bank of Italy.
[1] Current items (Group A) are on a transactions basis; all other items are on a payments (exchange record) basis. No sign indicates credit; minus sign indicates debit.
[2] Preliminary.
[3] Part of "Foreign investments in Italy" is believed to be financed from the proceeds of Italian banknotes remitted abroad and subsequently repatriated; to that extent foreign investment in Italy is overstated.

beginning of the year Italy was the major deficit country in the world, but by the third quarter it had become the major surplus country. During the crisis in the first quarter of the year, the Italian authorities were supported by foreign credits and similar facilities totaling about $1 billion, including $450 million of medium-term credits made available by the United States. When a surplus had been recovered they acted to prevent this from having undesirable repercussions on international liquidity: they did not, on balance, convert accruals of foreign currencies into gold but ordered the commercial banks to reduce their net foreign liabilities. Toward the end of the year, the Italian Government adopted economic policies that seemed likely to reduce, if not eliminate, the surplus.

The developments that led to the large balance of payments deficit in 1963 were described in last year's Annual Report. Essentially, rapid economic growth over a number of years, supported by steadily rising exports and large-scale emigration of labor to neighboring countries, had brought about strong pressures on wages and prices as the economy was reaching full employment conditions. These pressures were accompanied by a substantial excess demand in the economy in 1963 and 1964, and by a considerable shortfall of supply in domestic agriculture. Together, they both hampered the growth of exports and stimulated the sharp rise in imports. At the same time, the sharply rising incomes accentuated various structural problems of economic adjustment. To deal both with the domestic inflationary pressures and with the balance of payments deficit, the Italian authorities applied monetary and fiscal measures of increasing restraint, beginning in May 1963. In the course of 1964 these measures proved effective in correcting the balance of payments, but appeared to be somewhat less effective in reducing pressures on prices and wages, although some progress in that respect was recorded. They also resulted in a decline in industrial production. The adjustment in the balance of payments was undoubtedly facilitated by the generally buoyant international demand.

The measures applied acted both on the current and the capital account. Exports rose at a substantial rate throughout 1964, while imports tended to fall until the last quarter. A better harvest than in the two preceding years also contributed to the reduction in the trade deficit. Capital transactions (other than changes in commercial bank assets and liabilities) turned from a large outflow into a large inflow, under the influence of both the restrictive monetary policies and the restoration of confidence, which had been much impaired during the period of the large deficits.

Even though the surplus in the second half of 1964 was exceptionally large, there was no clear evidence that the Italian balance of payments was returning to a period of persistent surplus accompanied by rapid economic growth.

Japan

In the postwar period Japan, while maintaining a very high rate of long-term growth, has experienced a series of domestic booms and recessions, which have had pronounced secondary effects on the balance of payments. Severe difficulties in 1961 were met by corrective measures which slowed for a time the steep rise in domestic production. However, recovery was rapid, and by the middle of 1963 a balance of payments problem again began to emerge. On this occasion measures were taken to restrain the boom rather earlier than had previously been done, and tight money measures were introduced at the end of 1963 which markedly slowed the rate of increase in imports. A rapid rise in exports, supported both by strong international demand and by the high degree of competitiveness of Japanese industry, helped to smooth the adjustment; during 1964 the balance of payments recovered while economic growth was moderated, but was not interrupted, as it had been in 1958 and 1962. At the end of the year the Japanese authorities began to relax their policies of economic restraint.

Japan's deficit on account of goods and services and private transfers was much reduced from 1963 to 1964 (Table 36). The improvement came in the second half of the year; after allowing for seasonal factors there was then a small surplus on current transactions, compared with a seasonally adjusted deficit of about $450 million in the first half of the year. Exports expanded steadily throughout the year, totaling

TABLE 36. JAPAN: BALANCE OF PAYMENTS SUMMARY, 1963–FIRST QUARTER 1965[1]

(In millions of U.S. dollars)

	1963	1964[2]	1964[2] First quarter	1964[2] Second quarter	1964[2] Third Quarter	1964[2] Fourth quarter	1965[2] First quarter
A. Goods, Services, and Private Transfer Payments							
Exports f.o.b.	5,391	6,706	1,317	1,580	1,736	2,073	1,822
Imports f.o.b.	—5,557	—6,358	—1,621	—1,640	—1,488	—1,609	—1,614
Trade balance	—166	348	—304	—60	248	464	208
Government special receipts[3]	356	329	77	83	81	88	71
Other services and private transfer payments	—884	—1,066	—293	—270	—249	—254	—300
Total	—694	—389	—520	—247	80	298	—21
B. Private Long-Term Capital							
Direct investment	—21	54	16	20	21	—3	16
Other	528	77	79	3	37	—42	8
Total	507	131	95	23	58	—45	24
C. Central Government Transfer Payments and Nonmonetary Capital							
Reparations and loans extended	—125	—108	—26	—18	—35	—29	—33
IBRD loans received (net)	32	1	4	—	—	—3	2
Other[4]	—32	—11	—27	35	—23	4	—17
Total	—125	—118	—49	17	—58	—28	—48
D. Total (A through C)	—312	—376	—474	—207	80	225	—45
E. Net Errors and Omissions	44	—4	31	—34	45	—46	20
F. Private Short-Term Capital							
Nonmonetary sector	107	253	171	—14	36	60	—10
Commercial banks							
Liabilities	848	669	267	247	45	110	144
Assets (increase —)	—438	—598	—57	—101	—217	—223	—50
Total	517	324	381	132	—136	—53	84
G. Treasury and Bank of Japan Monetary Capital and Gold							
IMF position	—	—40	—	—	—	—40	—3
Liabilities[4]	—226	9	1	53	—2	—43	—
Payments agreement assets	14	8	—1	—4	16	—3	—5
Official reserves (increase —)	—37	79	62	60	—3	—40	—51
Total	—249	56	62	109	11	—126	—59

Source: Data provided by the Japanese authorities.
[1] No sign indicates credit; minus sign indicates debit.
[2] Preliminary.
[3] Including sales to U.S. and UN forces under the special procurement program.
[4] Yen subscription, other than the amount immediately converted into dollars, to the International Development Association ($6.1 million for 1963) and the corresponding increase in liabilities are excluded from this table.

about one fourth more than in 1963. Imports, which in the first half of the year had been running 25 per cent above the figure for the same period of 1963, were only 14 per cent higher for the year as a whole. This resulted in a swing in the trade balance from a deficit in 1963 to a substantial surplus in 1964. The deficit on goods and services account was nearly halved.

The inflow of private long-term capital into Japan in 1964 was markedly reduced owing to uncertainties concerning Japan's prospects of obtaining exemption from the U.S. Interest Equalization Tax. During 1964 Japan did not place any new issues in the U.S. market, but borrowed in Europe; the inflow of private capital fell by about $370 million, more than offsetting the improvement in the balance on current account. As a result the deficit on current and long-term capital account increased to $376 million. However, this deficit was for the most part matched by an inflow of short-term capital, reserves showing little change. Net borrowing by the commercial banks played only a minor role; during the second half of 1964, the commercial banks built up their foreign assets by more than the rise in their foreign liabilities, improving their net position by close to $300 million. For the year as a whole their net positions deteriorated only by $71 million, compared with more than $400 million in 1963. This development presumably reflected both the improved trade balance (some assets representing export credits, and a large part of liabilities representing import usance bills) and measures of monetary policy.

The improvement in the balance of payments continued into the early months of 1965, when the current account showed the lowest first-quarter deficit for several years. Although seasonal factors are adverse in this quarter, there was a considerable increase in exports over the same period in 1964. The inflow of private capital was renewed, although at a much lower level than in the first quarter of the previous year, and the reserve position improved by almost $60 million.

Australia

The Australian balance of payments became less favorable in the course of 1964, though it was in surplus for the year as a whole (Table 37). A substantial increase in volume contributed to a 9 per cent increase in the value of exports over 1963, but imports rose throughout the year and were more than 20 per cent higher in 1964 than in the previous year. As a result, the trade surplus was reduced by some $250 million. The current account deficit, at about $420 million, was the highest since 1960. There was, however, another heavy inflow of capital, so that reserves rose for the fourth successive year, to $1,847 million. Export prices, which had risen sharply in 1963, reached a peak in the first quarter of 1964 but declined thereafter, largely because of a steady decline in wool and sugar prices after March and a fall in wheat prices in the later part of the year. However, prices of meat and metals were higher in 1964 than in 1963. Wheat exports to countries in the Sino-Soviet area again played an important role in expanding exports.

TABLE 37. AUSTRALIA: BALANCE OF PAYMENTS SUMMARY, 1961-64[1]

(In millions of U.S. dollars)

	1961	1962	1963	1964
A. Goods, Services, and Transfer Payments				
Exports f.o.b.	2,314	2,334	2,761	2,995
Wool (at current prices)	*815*	*827*	*972*	*1,006*
Wool (at 1958 prices)	*768*	*773*	*766*	*793*
Wheat (at current prices)	*352*	*284*	*367*	*408*
Wheat (at 1958 prices)	*370*	*280*	*367*	*385*
Imports f.o.b.	—2,003	—2,178	—2,328	—2,800
Trade balance	311	156	433	195
Investment income	—245	—248	—293	—278
Other services and transfers	—282	—272	—315	—338
Total	—216	—364	—175	—421
B. Private Capital (including errors and omissions)	526	469	671	513
C. Official Capital	21	35	—6	—27
D. Total (A through C)	331	140	490	65
E. Monetary Movements				
IMF position	175	—176	—26	—
Official and banking reserves (increase —)	—506	36	—464	—65
Total	—331	—140	—490	—65

Source: Based on data from the Commonwealth Statistician.
[1] No sign indicates credit; minus sign indicates debit.

The continued rise in export earnings has, over the last two or three years, helped to support a substantial rate of economic growth and a high level of employment; real gross national product rose by about 6 per cent in 1964 and unemployment fell to about 1 per cent of the labor force. During the year demand pressures emerged in some areas of the economy, and since March 1964 domestic prices have been rising at a rate of about 4 per cent a year. The budget for the fiscal year ended June 1965 was designed to prevent an excessive rise in domestic demand and included a substantial increase in tax rates. In order to contain the increase in the money supply and discourage any marked change in liquidity preference, action has been taken to raise interest rates, and reserve requirements for the commercial banks at the Reserve Bank were increased on several occasions, although some reductions were subsequently made to allow for seasonal movements in the banks' liquidity. In the first quarter of 1965 the balance of payments showed a considerable deficit. Exports were slightly below the level of the first quarter of 1964, while imports increased still further. Reserves dropped sharply and, at the end of the quarter, were $1,669 million.

Brazil

In most of the years since World War II, but particularly in recent years, persistent inflation in Brazil was accompanied by great pressure on the balance of payments. During 1964 the rate of inflation moderated somewhat, while remaining high for the year as a whole, and in that year, for the first time in more than a decade, the current account of the balance of payments was brought into surplus (Table 38). Within the current account the trade surplus trebled, owing mainly to a reduction in imports by almost 17 per cent, resulting in part from a further depreciation of the cruzeiro; exports rose only slightly.

Despite the improvement in the merchandize accounts there was a further build-up of import payment arrears until September 1964. Subsequently these arrears were reduced, and by April 1965 they had been eliminated.

The problems of servicing a rising foreign debt appear to have induced some further decline in 1964 in the inflow of foreign capital. However, debt rescheduling agreements reached during the year, together with other action taken by the authorities, appear to have improved the climate for a renewed capital inflow.

TABLE 38. BRAZIL: BALANCE OF PAYMENTS SUMMARY, 1961-64[1]

(In millions of U.S. dollars)

	1961	1962	1963	1964[2]
A. Goods, Services, and Transfer Payments				
Exports of coffee f.o.b.	710	643	748	760
Other exports f.o.b.	695	572	658	670
Imports f.o.b.	—1,292	—1,304	—1,294	—1,080
Trade balance	113	—89	112	350
Services	—416	—407	—333	—282
Transfer payments	15	38	39	20
Total	—288	—458	—182	88
B. Miscellaneous Capital and Net Errors and Omissions	124	46	—51	—41
C. Total (A plus B)	—164	—412	—233	47
D. Loans, Payments Agreements and U.S.P.L. 480 Aid, Swaps, and Import Arrears				
Drawings on loans	799	481	445	331
Repayments on loans	—326	—310	—364	—286
Lines of credit and swaps	—38	7	—41	—50
Other import financing (including net payments agreements)	—55	18	36	104
Import arrears	—69	165	33	36
Total	311	361	109	135
E. Monetary Movements				
IMF position	40	—18	5	—28
Central Bank net foreign exchange assets (increase —)	—127	19	34	—194
Monetary gold (increase —)	2	60	76	59
Commercial banks' net assets (increase —)	—62	—10	9	—19
Total	—147	51	124	—182

Source: Based on data from the Central Bank of Brazil.
[1] No sign indicates credit; minus sign indicates debit.
[2] Preliminary.

At the end of 1963, the outstanding principal on medium-term and long-term indebtedness registered with the Brazilian monetary authorities amounted to approximately $2.5 billion. Scheduled payments on these debts for 1964 and 1965, including interest, totaled about $1 billion. This prompted the authorities, early in 1964, to begin a series of negotiations with the major creditor countries for a rescheduling of repayments. The resulting agreements provide that Brazil should meet in full as they fall due in 1964 and 1965 suppliers' credits guaranteed by the foreign Governments participating in the agreement, but that 70 per cent of the total should be refinanced by the Governments concerned. A comprehensive financial program, and important institutional reforms, including the setting up of a central bank, were submitted to the Fund toward the end of 1964. In the field of public finance, the program included new tax measures and restraint in expenditures, better administrative control over government expenditure, and periodic adjustments in the rates for public utility services. Policies for the private sector included allowing the price mechanism to play a wider role and thus gradually eliminating the existing serious distortions, a vigorous stimulus to exports, a firmer control of bank credit, a flexible exchange rate to ensure a better performance of the balance of payments, liquidation of commercial arrears, and measures designed to encourage an inflow of official and private foreign capital to assist in the development of Brazil's vast economic potential. In January 1965 Brazil concluded a stand-by arrangement with the Fund; details are given on page 109.

Ghana

The balance of payments deficit that has persisted in Ghana since 1959 reflects an excess of domestic demand originating largely in the public sector. A part of this excess demand has been deliberate, representing a preparedness to draw down reserves for purposes of economic development; but another part has resulted from the fact that the Government's budgeted expenditures were predicated on expectations regarding cocoa export proceeds which did not materialize because of the fall in cocoa prices; the world price of cocoa fell from an average of £336 a ton in

1958 to £179 a ton in 1964 and to £122 in April 1965. On the other hand, output of cocoa in Ghana has increased substantially in recent years—from 264,000 long tons in 1956/57 to a plateau of 400,000-450,000 tons in the early 1960's and to some 550,000-600,000 tons today. In fact, Ghana's receipts from cocoa exports, as shown in Table 39, have remained relatively stable in recent years. The price paid to the cocoa farmers has not been reduced commensurately with the fall in world prices, and the income of the cocoa farmers has increased with the rise in output, expanding domestic demand.

TABLE 39. GHANA: BALANCE OF PAYMENTS SUMMARY, 1961-64[1]

(In millions of U.S. dollars)

	1961	1962	1963	1964[2]
A. Goods, Services, and Transfer Payments				
Exports of cocoa f.o.b.	194	188	191	191
Other exports f.o.b.[3]	139	132	114	130
Imports f.o.b.	—385	—310	—331	—312
Trade balance	—52	10	—26	9
Services	—78	—73	—78	—72
Transfer payments	—15	—14	—16	—22
Total	—145	—77	—120	—85
B. Private Capital and Net Errors and Omissions	—30	14	4	16
C. Central Government Misc. Capital (excl. Group D)				
Loans and commercial credits received (net)	32	35	32	39
Other	—67	10	5	6
Total	—35	45	37	45
D. Monetary Movements				
IMF position	—	14	—	—
Sterling assets (increase —)				
Commercial banks (net)	10	14	10	—6
Cocoa Marketing Board and other official entities	78	—	26	9
Central government	92	2	8	—6
Central bank and currency reserves	30	—12	35	27[4]
Total	210	18	79	24

Source: Based on data from the Bank of Ghana.
[1] No sign indicates credit; minus sign indicates debit.
[2] Preliminary.
[3] Including nonmonetary gold.
[4] Including an increase in official liabilities (credit of $22 million).

Until 1962 the excess demand spilled over in higher imports ($385 million in 1961). From 1962 through 1964 imports were restricted to a level only slightly in excess of $300 million. The continuing current account deficits as well as, in certain years, a sizable capital outflow (e.g., to Guinea, Mali, and Upper Volta), were financed by borrowing abroad (mainly suppliers' credits), by drawing down reserves, and—in 1964—by borrowing against securities held in the reserves.

The outcome has been that Ghana's international reserves declined from some $530 million in 1957 to a total (net of securities pledged against short-term loans) of less than $70 million in the spring of 1965. In addition, Ghana has incurred a considerable foreign debt; suppliers' credits denominated in foreign currency arranged from 1959 to April 1965 totaled some £G 200 million ($560 million); by the latter date principal and interest totaling some £G 35 million had been paid.

Owing to a more rapid rise in expenditures (both recurrent and capital) than in revenue, the over-all deficit on the Government's budget rose to £G 50 million in 1962/63; it was reduced to £G 38 million in 1963/64, but is estimated at £G 66 million in 1964/65. The deficits have been financed by drawing down the overseas holdings of the Government and by the issue of Treasury bills. The rise in prices, as measured by the official index, has been more than 20 per cent over the last two years; there has been no apparent increase in wage rates. Shortages are occurring of certain essential foodstuffs, spare parts, and raw materials, reflecting the restrictiveness of the import licensing system and inadequate priorities.

India

India's surplus in 1964 was little larger than in 1963 (Table 40) despite greater use of external assistance and the continued tight restriction on imports and overseas payments. There was a major deterioration in the current account position, which may in part be attributed to internal developments, particularly the failure of foodgrain production during the last few years to meet the increase in consumption, resulting in a need for additional imports as domestic scarcities developed. In addition, pressures on the balance of payments were increased by import needs arising from expanded defense expenditures during 1962-64. In the second half of 1964, there was a particularly marked upsurge in domestic prices and a large increase in imports. Imports in 1964 rose by some 19 per cent while exports rose by

TABLE 40. INDIA: BALANCE OF PAYMENTS SUMMARY, 1961-64[1]

(In millions of U.S. dollars)

	1961	1962	1963	1964[2]
A. Goods, Services, and Private Transfers				
Exports f.o.b.	1,389	1,412	1,625	1,717
Imports mainly c.i.f.	—2,140	—2,288	—2,455	—2,915
Trade balance	—751	—876	—830	—1,198
Services	—41	—69	—7	—32
Private transfers[3]	57	47	71	58
Total	—735	—898	—766	—1,172
B. Private Capital and Net Errors and Omissions	—1	18	—59	—126
C. Official Transfers and Capital				
Transfers[3]	35	123	140	262
Capital	667	620	702	1,061
Total	702	743	842	1,323
D. Total (A through C)	—34	—137	17	25
E. Monetary Movements				
IMF position	126	29	—20	—44
Commercial banks	—25	—	6	—
Central institutions				
Other liabilities	—74	—8	13	1
Other assets (increase —)	7	116	—16	18
Total	34	137	—17	—25

Source: Based on data from the Indian authorities.
[1] No sign indicates credit; minus sign indicates debit.
[2] Preliminary.
[3] Grants of U.S. surplus agricultural commodities through private agencies are included with official transfers.

only 6 per cent, resulting in an increase of about $360 million in the trade deficit.

The deficit on current account, together with the net debit for private capital and net errors and omissions, was more than offset by increases in net official receipts of capital and transfer payments. Net official transfers received increased by about $120 million to $260 million, a level seven times that received three years earlier, while net official capital receipts increased by almost $360 million. In spite of these increases in aid receipts, India continues to receive considerably less aid per capita than most other developing countries. Moreover, the heavy official borrowing of recent years has resulted in a debt servicing problem; in 1964 such payments amounted to about 12 per cent of exports.

The seriousness of the balance of payments position necessitated the taking of several anti-inflationary steps towards the end of 1964, including an increase in the bank rate and a markup of interest rates generally. Despite this, the external position deteriorated and by early in 1965 reserves had fallen to the unprecedentedly low total of $480 million. Two special factors aggravated the reserves position at that time. First, the inflow of foreign banking funds that normally occurs in the busy season in India's money market (November-April) was much smaller in 1964/65. Second, there were delays in the normal discounting of export bills abroad and in the repatriation of proceeds of bills that were discounted. (This is part of the explanation for the enlarged debit in 1964 on account of errors and omissions.)

Further steps, therefore, had to be taken in early 1965 to restrain domestic monetary expansion and to ease the pressure on the balance of payments. The bank rate was further increased, and the budget for the fiscal year which began on April 1 was designed to reduce greatly recourse to bank financing. An additional regulatory duty of 10 per cent on all but the most essential imports was also introduced. In March a $200 million stand-by with the Fund was approved, against which several drawings have been made.

TABLE 41. MEXICO: BALANCE OF PAYMENTS SUMMARY, 1961-64[1]

(In millions of U.S. dollars)

	1961	1962	1963[2]	1964[3]
A. Goods, Services, and Private Transfers				
Exports f.o.b.	839	941	986	1,071
Imports mainly c.i.f.	—1,143	—1,155	—1,248	—1,499
Trade balance	—304	—214	—262	—428
Travel	269	275	307	324
Other services	—180	—217	—244	—285
Private transfers	—14	—17	—16	—4
Total	—229	—173	—215	—393
B. Private Capital (including commercial bank loans) and Net Errors and Omissions	36	252	261	358 (B and C)
C. Official Transfers and Capital	134	—11	85	
D. Total (A through C)	—59	68	131	—35
E. Commercial Banks' Short-Term Capital	32	—59	—8	80
F. Reserve Movements				
IMF position	45	—45	—	—
Bank of Mexico				
Other liabilities	—3	6	—3	3
Other assets (increase —)	—15	30	—120	—48
Total	27	—9	—123	—45

Source: Based on data from the Bank of Mexico.
[1] No sign indicates credit; minus sign indicates debit.
[2] Provisional.
[3] Preliminary.

Mexico

Mexico's net international reserves (including its position in the Fund) rose in 1964 for the third successive year. There was again a large inflow of capital, which more than offset the deterioration in the balance on current account (Table 41). The latter was due mainly to a rise in the trade deficit, although there was also a decline in the net surplus on invisibles. Investment income payments abroad rose sharply in 1964, while net travel receipts, which have shown substantial gains in the past decade, increased at a somewhat slower rate, as travel expenditures abroad by Mexican residents increased more rapidly than receipts from tourism.

The increase in the trade deficit was caused by a 20 per cent growth in imports while exports advanced by 9 per cent. In large part, the expansion of imports reflected the upsurge in the inflow of capital, including foreign loans to the Government and to government enterprises. There was also a substantial inflow of commercial bank short-term capital. Increased exports of coffee, wheat, corn, sugar, and some minerals more than offset lower exports of cotton (the most important export product of Mexico) and of manufactures. The decline in cotton exports was caused by a reduction in output, but the reduction in exports of manufactures was due to a substantial expansion in internal demand, which absorbed more than the increase in domestic production.

Since 1961 Mexico has achieved an impressive improvement in the annual rate of growth in its real GNP—from 3.5 per cent to about 10 per cent in 1964. Considering the sharp advance in this rate of expansion, the increase in Mexican prices has been quite moderate.

Chapter 9

Gold

Gold Production

WORLD output of gold, excluding the production of the U.S.S.R., Mainland China, and countries associated with them, increased in 1964 for the eleventh consecutive year. The increase of about 3.4 per cent carried total production to the highest figure ever reached, about 40 million ounces, worth (at $35 a fine ounce) approximately $1,400 million (Table 42). This was almost entirely the result of increased production in South Africa. The comparable figure for the value of output in 1963 was $1,354 million; in 1962, $1,300 million; in 1961, $1,215 million; and in 1960, $1,178 million. The gold mining industry in South Africa again established new records; its production increased by more than 1.7 million ounces (6.2 per cent) to a total of 29.1 million ounces, equivalent in value to $1,020 million. This output constituted approximately 73 per cent of world production.

The number of tons of ore milled in South Africa in 1964 was about 1.5 per cent greater than in 1963, and the average grade of ore per ton milled rose from 6.861 dwt. in 1963 to 7.185 dwt. in 1964. By 1951 the average grade of ore had fallen to 3.756 dwt., but it has improved steadily since that time. Combined working profits from gold, uranium, and other products rose from R 313.0 million ($438.2 million) in 1963 to a record figure of R 332.6 million ($465.6 million) in 1964.

The value of production increased also in the Democratic Republic of Congo by the equivalent of $2.0 million, to $9.5 million, and in Colombia, India, Japan, and Rhodesia by lesser amounts, raising the value of production in these countries to the equivalents of $13.1 million, $5.2 million, $16.1 million, and $20.1 million, respectively. Gold production also increased sharply in the Philippines, where output was 13.3 per cent higher than in 1963, being equivalent to $14.9 million. This increase has been attributed mainly to the resumption of normal operations by a major company which suffered loss of production because of a prolonged strike in 1963, to the extension to 1967 of the Gold Assistance Act, and to tax exemption granted to certain mines.

TABLE 42. GOLD: VALUE OF WORLD PRODUCTION, 1940, 1945, AND 1960-64[1]

(In millions of U.S. dollars at US$35 a fine ounce)

	1940	1945	1960	1961	1962	1963	1964
South Africa	492	428	748	803	892	961	1,020
Canada	186	95	162	155	145	139	133
United States	170	32	59	55	55	51	51
Australia	57	23	38	38	38	36	34
Ghana	31	19	31	29	31	32	30
Rhodesia	29	20	20	20	19	20	20
Japan	30	3	12	13	15	15	16
Philippines	39	—	14	15	15	13	15
Colombia	22	18	15	14	14	11	13
Congo, Dem. Rep. of	20	12	11	8	7	7	9
Mexico	31	17	11	9	8	8	7
Other[2]	157	69	57	56	61	61	52
Total[2]	1,264	736	1,178	1,215	1,300	1,354	1,400

Source: International Monetary Fund, *International Financial Statistics.*

[1] Excluding the output of countries in the Sino-Soviet area.

[2] These figures include estimates for data not available.

Production in Canada declined again in 1964, falling to 3.8 million ounces, equivalent to US$133.0 million; this was the smallest output since 1948, when it totaled 3.5 million ounces (US$123.9 million). The 1964 figure compares with 4.0 million ounces (US$139.0 million) in 1963 and 4.2 million ounces (US$145.5 million) in 1962. The year of peak output in Canada was 1941, when 5.4 million ounces (US$188.0 million) were mined. In Canada, as elsewhere, costs of production in the gold mining industry have been rising. Production from new sources is thought unlikely to offset the declining output resulting from the closure of mines that are reaching the end of their reserves.

In the United States, whose output is the next largest to that of Canada (if the U.S.S.R. is disregarded), production declined again, to approximately 1.4 million ounces ($50.6 million), from 1.5 million ounces ($51.4 million) in 1963, after having been about 1.6 million ounces ($55 million) in both 1961 and 1962. The peak year for the United States was 1940, when 4.9 million ounces, equivalent to $170 million, were produced. Australia's gold production continued to decline in 1964, amounting to approximately 1 million ounces ($34 million). In 1963, output had been 1.03 million ounces ($36 million) after it had remained steady at about 1.09 million ounces ($38 million) in 1960, 1961, and 1962. Production also declined in Ghana, by the equivalent of $2.0 million, to $30.2 million; in Mexico by $0.9 million, to $7.4 million; and in Nicaragua by $0.2 million, to $6.9 million.

Gold has become Bolivia's fourth largest export, and production has increased steadily over the past few years. A recent geological survey estimated the gold reserves in northeastern La Paz at between $1 billion and $3 billion. It has been estimated that, with modern techniques, Bolivia could be producing gold valued at approximately $22 million yearly by 1972. In southern India, the Geological Department of Kerala State has begun investigations of gold deposits in parts of the Kozhikode district. It has also been reported that gold can be extracted on a profitable basis from the deposits in South Wynaad and Nilambur areas.

Sales of gold by the Soviet Union, totaling the equivalent of approximately $330 million in the early months of 1964, have drawn further attention to Russian gold production. These sales, understood to be prompted by a need for foreign exchange in connection with grain purchases, compare with sales equivalent to $550 million in 1963 and $215 million in 1962. The official Russian news agency, Tass, has asserted that Russian gold sales in 1963 did not deplete that country's gold reserves. A member of the Soviet State Geological Committee has claimed that a large new gold field, which has been discovered on the Kolyma River in the Yakutsk region, could be the biggest in the world. Another report from the East German news agency, ADN, mentioned new gold discoveries in Central Asia, Kazakhstan, and Transcaucasia, which are estimated to be able to produce as much gold as all the east and northeast regions of Russia produce at present. It has also been reported that modern machinery and mining methods are now being employed to increase production.

In general, the gold mining industry remains concerned by the decreasing gap between rising costs of production and the fixed price of $35 a fine ounce. Several governments have granted assistance to their gold mining industries; in some countries this assistance has taken the form of subsidies. These arrangements are mentioned below.

Gold Holdings

The monetary authorities of the world are estimated to have added about $725 million in 1964 to their stocks of gold (Table 43 and Chart 28); this compares with additions of about $840 million in 1963, $330 million in 1962, $600 millon in 1961, and $225 million in 1951, the year in which the smallest postwar increase was recorded. The holdings of the Sino-Soviet area have not been included in these figures, but those of the International Monetary Fund, the Bank for International Settlements, and the European Fund have been taken into account. World reserves of monetary gold, thus defined, amounted to the equivalent of approximately $43 billion. The important movements in the distribution of reserves during 1964 are discussed in Chapter 6.

The amount of newly available gold in the

CHART 28. GOLD: ESTIMATED SUPPLY AND ABSORPTION, 1951-64

(In millions of U.S. dollars)

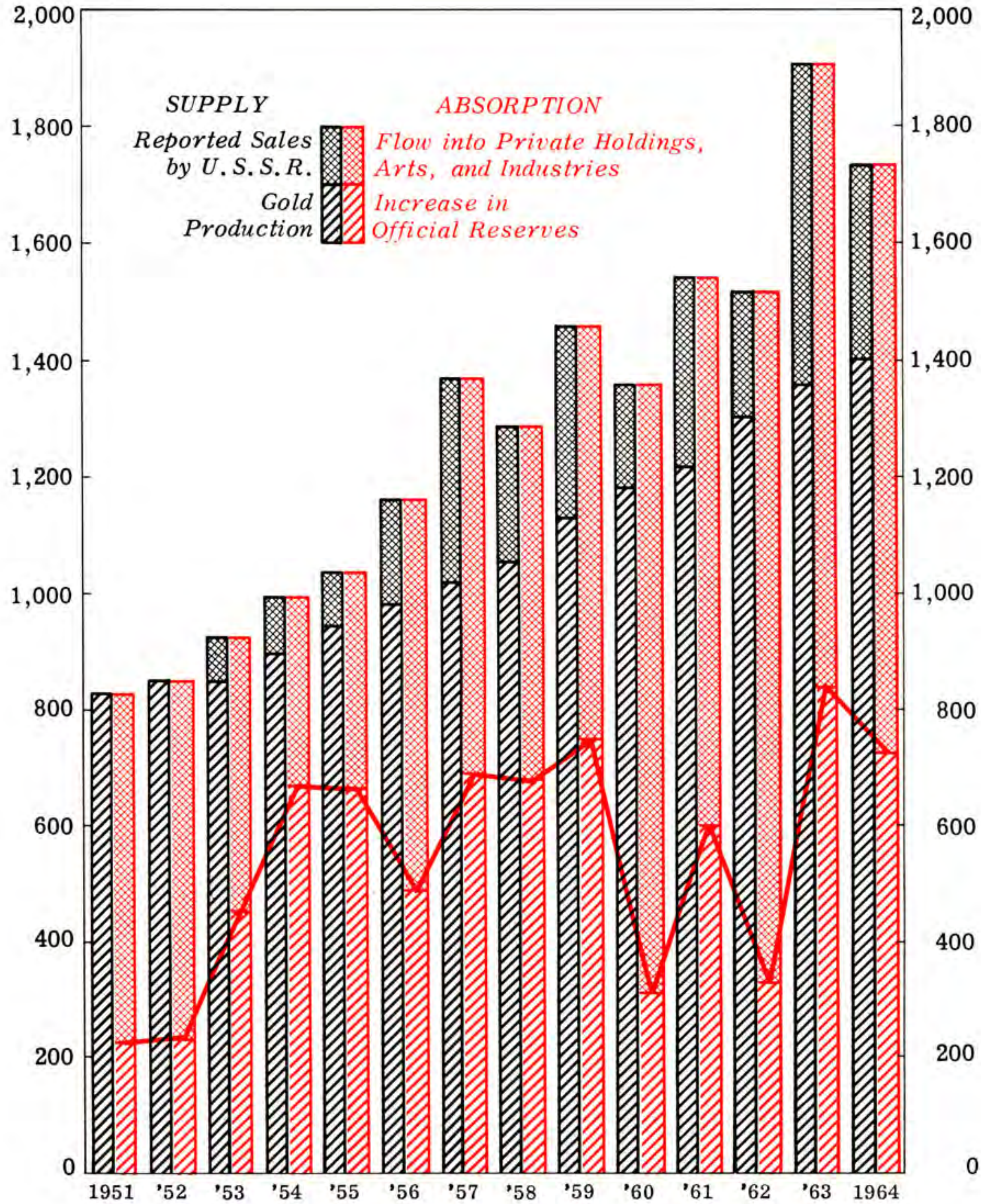


TABLE 43. WORLD GOLD RESERVES: SOURCES OF CHANGES, 1962-64

(In millions of U.S. dollars)

	1962	1963	1964
Production	1,300	1,354	1,400
Soviet sales	215	550	330
Total available	1,515	1,904	1,730
Consumption in industry and arts, and private hoarding	−1,185	−1,064	−1,005
Total added to world monetary gold stock[1]	330	840	725
IMF gold transactions			
Subscriptions	−25	−45	−71
Sales to countries	—	—	250
Repayments	−67	−49	−20
Charges	−25	−24	−27
BIS and EF gold transactions	165	238	−225
Total added to countries' monetary gold stock[1, 2]	380	960	635

Sources: International Monetary Fund, *International Financial Statistics*, and Fund staff estimates.
[1] Excluding stocks held by countries in the Sino-Soviet area.
[2] Totals do not equal the sums of the items because of rounding.

Western world in 1964 was of the order of the equivalent of $1,730 million. Absorption by private holders, industry, and the arts in 1964 thus appears to have been in the region of $1,005 million, i.e., some $60 million less than in 1963.

Gold Markets and Prices

New York

As fiscal agent for the U.S. Treasury, the Federal Reserve Bank of New York stands ready to buy gold at the price of $34.9125 a fine ounce and to sell gold at $35.0875 a fine ounce for official monetary purposes. In 1964, it sold gold equivalent to $36.2 million (net) to foreign countries and international institutions. In addition, the equivalent of $89.0 million was sold domestically for industrial, professional, and artistic uses. The total decrease in the U.S. gold stock during the calendar year 1964 thus amounted to some $125.2 million (Table 44), compared with $460.7 million in 1963 and some $889.9 million in 1962. Purchases of gold from foreign countries in 1964 included the equivalent of $617.7 million from the United Kingdom, of which approximately $300 million resulted from the United States' 50 per cent share in the operations of the Gold Pool, described in last year's Annual Report (p. 131).

The amount of gold held under earmark by the Federal Reserve Banks for account of foreign central banks, governments, and international institutions fell in 1964 by the equivalent of $255.3 million, to $12.7 billion. This fall was due primarily to the fact that in 1964 France repatriated in gold the equivalent of some $422 million.

TABLE 44. U.S. GOLD TRANSACTIONS, 1963 AND 1964

(In millions of U.S. dollars)

	1963	1964
Purchases from		
Brazil	72.2	54.2
Italy	—	200.0
United Kingdom	329.3	617.7
Other countries	36.7	35.0
	438.2	906.9
Sales to		
Austria	82.1	55.4
Belgium	—	40.1
France	517.7	405.1
Germany, Fed. Rep. of	—	225.0[1]
Netherlands	—	60.0
Spain	130.0	32.0
Switzerland	—	81.0
Other countries	100.1	44.5
Industrial, professional, artistic	69.0	89.0
	898.9	1,032.1
Net decrease in stocks	460.7	125.2

[1] Two hundred million dollars of these sales formed part of the transaction initiated by the purchase from Italy shown.

London

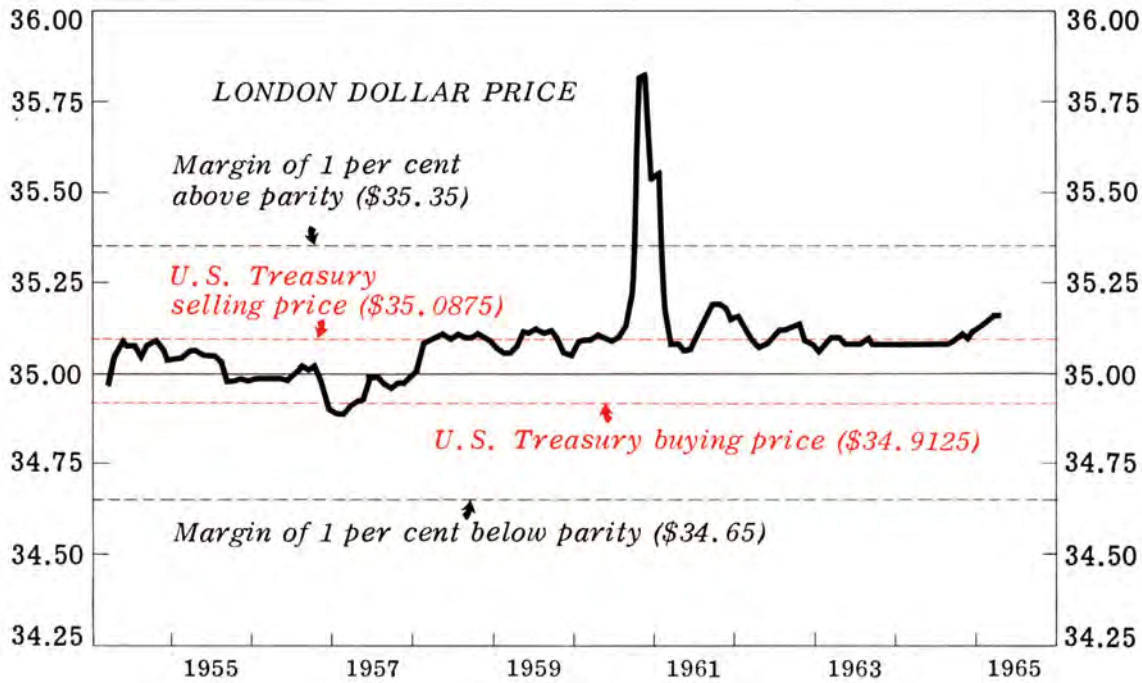
Over the period May 1, 1964 to April 30, 1965, the dollar price of gold (converted at the buying price for dollars in London at the time of the daily fixing) fluctuated within a range of about 11⅟₁₆ cents—between a maximum of $35.17¾ a fine ounce on March 5, 1965 and a minimum of $35.06¹¹⁄₁₆ a fine ounce on August 25, 1964 (Chart 29). In the same 12-month period in 1963/64 the corresponding range was 5⁵⁄₁₆ cents—between $35.11³⁄₁₆ and $35.05⅞ a fine ounce.

On May 1, 1964, the equivalent price at the "fixing" was slightly above $35.07⅜ a fine ounce and, although there was a steady demand for bar gold, the price did not fluctuate by much more than 1 cent either side of $35.08 until mid-September. During this period, the Gold Pool was able to acquire a modest amount of gold becoming available from new production. The heavy sales of gold by the U.S.S.R. in the first three months of the year were not, however, repeated. At the beginning of August, the attack on U.S. naval craft in the Gulf of Tonkin caused a flurry in the gold market, and on August 6 dealings were reported at about \$35.10 a fine ounce after the "fixing" at \$35.08 15/16 a fine ounce. During the summer the exchange rate for the pound sterling had been progressively easing and on August 27 the sterling price at the "fixing" was 252s. 0¼d. a fine ounce. This was the first time since July 25, 1961 that the sterling price of gold had exceeded 252s.

Private demand for gold remained modest during August but increased sharply in September and October, as the approach of elections in both the United States and the United Kingdom caused some nervousness in the markets. This nervousness was accentuated in October by the political news from Moscow, reports of a worsening situation on the Malaysian/Indonesian border, and the news of the success of Mainland China's first atomic explosion. Following the results of the British elections on October 16, the demand for gold, coupled with a weakness of sterling in the exchange market, pushed the sterling price at the "fixing" to 252s. 4¾d. a fine ounce, the highest point of the year, and the U.S. dollar equivalent price to about \$35.12 3/16 a fine ounce, the highest price in U.S. dollar terms since the Cuban crisis in October 1962. While the authorities effectively controlled the market through the operations of the Gold Pool, speculation against the pound sterling persisted, and on November 23 the bank rate in London was raised from 5 per cent to 7 per cent. The sterling price at the "fixing" on November 23 was lower by 6¼d., reflecting an improvement in the dollar/sterling exchange rate, but speculation persisted and massive international support was mustered in defense of the existing parity of the pound. During this exchange crisis, the gold market had been fairly active but was not much affected by events in the exchange market. In mid-December, demand for hoarding was noticeable, and at the end of the year there was some covering of positions for balance sheet purposes.

CHART 29. GOLD: PRICE IN LONDON MARKET, MONTHLY AVERAGES, MARCH 1954–APRIL 1965

(In U.S. dollars a fine ounce)



A strong wave of buying started in January 1965, when there were rumors of the intention of the U.S. authorities to remove the gold reserve requirement against deposits in the Federal Reserve Banks and against Federal Reserve notes, and some publicity was given to the French intention to convert surplus dollars into gold. On January 8 there was a larger turnover of gold in London than on any day during the Cuban crisis. The "fixing" price was equivalent to nearly $35.15 a fine ounce, and the authorities met demand later in the day at prices up to $35.19 a fine ounce. Demand abated only after the U.S. Treasury issued a firm statement of its intention to maintain the existing price of gold. For the remainder of January, the price remained at about $35.12 a fine ounce, but demand again escalated early in February, on the appearance of French proposals for a reform of the international monetary system. The deteriorating situation in Viet-Nam caused some buying by speculators and others, and the price increased steadily until March 5, when at the "fixing" it reached, in U.S. dollar terms, a peak of slightly above $35.17¾ a fine ounce. On March 3, President Johnson signed the bill eliminating the requirement of a gold cover for Federal Reserve Bank deposits, thus freeing some $5 billion of gold to meet potential foreign claims. This measure had little immediate impact on a market overshadowed by events in Southeast Asia; nevertheless, with minor fluctuations, the price of gold in London declined steadily until April 30, when the price, in U.S. dollar terms, at the "fixing" was $35.10⅝ a fine ounce.

The Gold Pool continued to operate effectively and to exert a stabilizing influence in the market during 1964. Increased new production, plus substantial sales of gold by the U.S.S.R. in the first three months of the calendar year, enabled the Pool to share out the equivalent of some $600 million of gold to its participants, an amount similar to that distributed in 1963. No contributions to the Pool had to be made in 1964 by participating central banks.

During 1964, the United Kingdom imported some 40.9 million ounces of gold bullion, equivalent to $1,429.8 million, compared with 34.3 million ounces ($1,200.5 million) in 1963 and 34.1 million ounces ($1,192.9 million) in 1962. Of the imports in 1964, the equivalent of $1,106.0 million came from South Africa and the equivalent of $268.6 million from the U.S.S.R. These figures compare with $816.1 million and $281.2 million in 1963, and with $664.7 million and $106.9 million in 1962. Exports from the United Kingdom amounted to 17.6 million ounces, equivalent to $615.8 million, whereas in 1963 the total was 19 million ounces ($664.5 million), and in 1962 it was 29 million ounces ($1,013.8 million).

Other Developments

In markets where gold is bought and sold against local currencies (Table 45), the day-to-day movements of the U.S. dollar equivalent prices have varied from the London pattern because of the special characteristics of each market and the fluctuations in the intermediary rate of exchange. Prices for bar gold and gold coins in local currencies in the period May 1, 1964 to April 30, 1965 rose steadily under pressure from speculators because of the unsettled situation in Southeast Asia and other political uncertainties.

In Bombay, the U.S. dollar equivalent price for bar gold fluctuated quite widely. From a low point of $74.33 a fine ounce in the week ended May 8,

Table 45. Gold: Prices in Various World Markets, End of April 1964 and 1965

(In U.S. dollars a fine ounce, at day's dollar rate)

	Bar Gold		Sovereign		Napoleon	
	End of Apr. 1964	End of Apr. 1965	End of Apr. 1964	End of Apr. 1965	End of Apr. 1964	End of Apr. 1965
Beirut	35.32	35.28	41.55	42.33	45.26	46.37
Bombay	74.05[1]	84.30	—	—	—	—
Brussels	35.16	35.21	41.08	41.90	—	—
Hong Kong	38.09	39.88	—	—	—	—
Milan	35.44	35.45	42.15	42.15	50.58	51.45
Paris	35.20	35.27	41.35	42.02	46.24	48.18

[1] Average for week ended April 24. This figure was obtained by conversion from quotations for 14-carat gold; transactions are limited to gold of that purity.

1964, it rose to \$81.24 a fine ounce at the end of August 1964, but then fell sharply to \$74.23 a fine ounce in the week ended September 18. It would appear that the reduced demand for gold at this point reflected the gold control measures that the Indian Government had previously introduced.[1] (The number of dealers and refiners had fallen from about 27,000 to some 12,000, the quantity of gold used for industrial purposes had been reduced by approximately 50 per cent, and loans of scheduled banks against the security of gold had dropped from a peak of Rs 420 million [\$88 million] in October 1962 to Rs 180 million [\$38 million] in June 1964.) After September 18, the price of bar gold fluctuated narrowly but with an upward tendency, reaching \$84.30 a fine ounce in the week ended April 30, 1965.

The activity in the London gold market on January 8, 1965 was reflected in Paris, where the intervention of the authorities brought the price of the one-kilogram ingot down to F 5,640, from a peak of F 6,000, after what was described as an unprecedented demand for this type of bar gold. The turnover in Paris on January 8 was reported to be in the region of F 22.5 million (\$4.6 million).

In Hong Kong, trading in gold was reported to have been suspended temporarily at the end of the first week in March 1965 after the price had been forced up to HK\$271 an ounce, 0.945 fine, equivalent to about US\$41 a fine ounce.

Gold Transactions Service

Since the inauguration of the Fund's gold transactions service in March 1952, the central banks of 26 member countries and 5 international organizations have purchased or sold gold through the facilities provided by the Fund. In all, 120 transactions, amounting to about \$1,093 million, have taken place since March 1952. Although the creation of the Gold Pool has had the effect of virtually eliminating the need for the service, one transaction for the equivalent of approximately \$10 million was completed in the year under review, and the Fund received two or three inquiries as to whether it was aware of any sellers of gold.

[1] See *Annual Report, 1964,* page 108.

Changes in National Policies Affecting Gold

In *Argentina,* the Central Bank suspended trading in gold coins and bullion on June 15, 1964.

In the *United States,* the Secretary of the Treasury issued an order, effective on April 25, 1964, removing the restrictions on the holding of U.S. gold certificates issued before January 30, 1934. These certificates, at the time of their issuance, were redeemable in gold. By his order of December 28, 1933, as supplemented and amended by his orders of January 15, 1934 and July 14, 1954, the Secretary of the Treasury required the delivery to the United States of gold bullion, gold certificates, and gold coins situated in the United States, except gold coins having a recognized special value to collectors of rare and unusual coins. By virtue of a general license, all persons subject to the jurisdiction of the United States may now acquire, hold, dispose of, export, and import U.S. gold certificates issued before January 30, 1934, whether situated inside or outside the United States. Such certificates are not redeemable in gold, but may be exchanged at their dollar face value for other lawful U.S. coin or currency which is legal tender.

As stated above (p. 101), the requirement of a 25 per cent gold cover for deposits in Federal Reserve Banks has been eliminated. The statutory requirement regarding a 25 per cent gold cover for Federal Reserve notes was not affected, however.

In *Spain,* the Government decreed in April 1965 that gold bullion and gold coins required to be surrendered to the Government in 1937 could be handed back to private ownership because of the favorable evolution of the Spanish economy in recent years. Requests for the return of the gold are to be made to the Institute of Foreign Exchange; however, owners have been given the option of selling their gold to the Institute at the current price.

Gold Subsidy Programs

The gold subsidy programs of the Governments of Canada,[2] the Philippines,[3] South Africa,[4] and

[2] *Annual Report, 1959,* pages 149-50; *1961,* pages 125–26; *1964,* page 109.
[3] *Annual Report, 1962,* page 164; *1963,* page 181.
[4] *Annual Report, 1964,* page 109.

Rhodesia[5] discussed in previous Annual Reports have continued in operation during the past year. The gold subsidy program for the Philippines was extended, on the same terms and conditions, for a further three years until June 1967.

In *Australia,* as in most other gold-producing countries, rising production costs in conjunction with a fixed official price for gold have continued to create problems for the industry. The assistance which the Australian Government has been making available to the gold-mining industry in recent years has taken the forms of subsidies and development allowances. As the legislation authorizing this assistance was due to expire on June 30, 1965, the Australian Government recently reviewed the position of the industry and introduced new assistance arrangements. Under these arrangements the development allowance scheme has not been renewed and future assistance to the industry will be provided by continuing the subsidy scheme in a liberalized form. The liberalizations were designed to absorb to some extent the development allowance scheme into the subsidy scheme and to take account of the deterioration in the industry's general financial position since the Government last reviewed the question of assistance three years earlier. The new measures increased the maximum rate of subsidy for large producers from £A 3 5s. 0d. to £A 4 0s. 0d. per ounce, and the flat rate subsidy for small producers from £A 2 8s. 0d. to £A 3 0s. 0d. per ounce, with a consequential adjustment in the provision relating to the rate of subsidy payable to producers with an output of more than 500 ounces a year who elect to be treated as small producers. The legislation introducing the new arrangements provides that they will operate for a period of five years.

[5] *Annual Report, 1964,* page 109.
[6] *Annual Report, 1960,* page 144; *1963,* page 181.

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SUPPLEMENTARY NOTE

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Activities of the Fund

THIS note supplements the information given in Chapter 4 about the activities of the Fund during the past year.

Par Values

Initial par values were established by agreement between the Fund and three members during the fiscal year, as shown in Table 46.

TABLE 46. INITIAL PAR VALUES ESTABLISHED, FISCAL YEAR ENDED APRIL 30, 1965

Member	Effective Date	Units of Member's Currency per U.S. Dollar
Burundi	January 26, 1965	87.50000
Trinidad and Tobago	February 10, 1965	1.71429
Tunisia	September 28, 1964	0.52500

Article VIII Countries

It was noted earlier (p. 31) that Australia, Costa Rica, and Nicaragua have been added to the countries that have accepted the obligations of Article VIII, Sections 2, 3, and 4. The 27 countries that had accepted these obligations down to July 1, 1965 are listed in Table 47.

TABLE 47. COUNTRIES THAT HAVE ACCEPTED ARTICLE VIII

Member	Effective Date of Acceptance
Australia	July 1, 1965
Austria	August 1, 1962
Belgium	February 15, 1961
Canada	March 25, 1952
Costa Rica	February 1, 1965
Dominican Republic	August 1, 1963
El Salvador	November 6, 1946
France	February 15, 1961
Germany, Federal Republic of	February 15, 1961
Guatemala	January 27, 1947
Haiti	December 22, 1953
Honduras	July 1, 1950
Ireland	February 15, 1961
Italy	February 15, 1961
Jamaica	March 8, 1963
Japan	April 1, 1964
Kuwait	April 5, 1963
Luxembourg	February 15, 1961
Mexico	November 12, 1946
Netherlands	February 15, 1961
Nicaragua	July 20, 1964
Panama	November 26, 1946
Peru	February 15, 1961
Saudi Arabia	March 22, 1961
Sweden	February 15, 1961
United Kingdom	February 15, 1961
United States	December 10, 1946

Quotas

The quotas of 11 Fund members were increased during the fiscal year 1964/65. The countries concerned, their previous quotas, their new quotas, and the effective dates of their quota increases are shown in Table 48.

The increases for Jordan, Luxembourg, and Tunisia were the fifth, and final, installments of their quota increases by installments, to which they had consented under the 1959 Resolutions on the Enlargement of Fund Resources. The increase for Malaysia was the first of three equal installments by which its quota will be increased to $100 million. The increases for Ceylon, Costa Rica, Ghana, Iraq, and Sudan were approved under the terms of the Fund's Decision on the Compensatory Financing of Export Fluctuations, which provides that the Fund is willing to give sympathetic consideration to requests for quota adjustments from countries exporting primary products, especially those with relatively small quotas.[1]

During the fiscal year, four other quota increases under the terms of the Compensatory Financing Decision were approved by the Board of Governors: Guatemala, from $15 million to $20 million; Saudi Arabia, from $55 million to

[1] *Selected Decisions*, pages 40-43.

TABLE 48. INCREASES IN QUOTAS, FISCAL YEAR ENDED APRIL 30, 1965

(In millions of U.S. dollars)

Country	Effective Date	Previous Quota	New Quota
Ceylon	Apr. 7, 1965	45.00	62.00
Costa Rica	Jan. 11, 1965	15.00	20.00
Ghana	Feb. 23, 1965	35.00	55.00
Iraq	Mar. 4, 1965	15.00	55.00
Italy	Aug. 10, 1964	270.00	500.00
Jordan	July 13, 1964	9.60	11.25
Luxembourg	Sept. 17, 1964	14.00	15.00
Malaysia	Apr. 7, 1965	37.50	58.33
Panama	Feb. 10, 1965	0.50	11.25
Sudan	Mar. 17, 1965	15.00	45.00
Tunisia	June 3, 1964	20.40	22.50

TABLE 49. PURCHASES OF CURRENCIES FROM THE FUND, FISCAL YEAR ENDED APRIL 30, 1965

(In millions of U.S. dollars)

Members Purchasing	Under Stand-By Arrangements	Other	Total Purchases
Afghanistan		5.63	5.63
Brazil	50.00		50.00
Burundi	2.00		2.00
Ceylon		8.00	8.00
Chile	22.00		22.00
Colombia	5.00		5.00
Costa Rica	5.00		5.00
Cyprus		1.95	1.95
Dominican Republic	20.00		20.00
Ecuador	3.00		3.00
Haiti	3.75		3.75
Honduras	2.50		2.50
India	125.00		125.00
Iran		17.50	17.50
Israel		12.50	12.50
Liberia	3.30		3.30
Mali	9.90		9.90
Morocco		13.12	13.12
Nicaragua	5.65		5.65
Pakistan		16.00	16.00
Panama		2.69	2.69
Somalia	6.70		6.70
Sudan		7.50	7.50
Syrian Arab Republic	6.50		6.50
Tunisia	11.25		11.25
Turkey	16.00		16.00
United Arab Republic	40.00		40.00
United Kingdom	1,000.00		1,000.00
United States	475.00		475.00
Totals	1,812.55	84.89	1,897.44

$72 million; the Syrian Arab Republic, from $25 million to $30 million; and Thailand, from $45 million to $76 million. These increases become effective when the members concerned notify the Fund that they consent to the increases. In the period May 1-June 30, 1965, notifications were received from Guatemala, Saudi Arabia, and Thailand. In that same period the Board of Governors approved, under the terms of the Compensatory Financing Decision, increases in the quotas of Iraq, from $55 million to $64 million, and of Jordan, from $11.25 million to $12.25 million.

Fund Transactions

Table 49 lists the purchases of currencies from the Fund during the year, Table 50 the position

TABLE 50. POSITION OF PARTICIPANTS IN GENERAL ARRANGEMENTS TO BORROW

(In millions of U.S. dollars)

Participant	Maximum Amounts of Credit Arrange-ments	Amounts Borrowed by Fund: Dec. 1964	Amounts Borrowed by Fund: May 1965	Balance Available, May 31, 1965, Under Credit Arrange-ments
Belgium	150	30.0	37.5	82.5
Canada	200	15.0	35.0	150.0
France	550	100.0	140.0	310.0
Deutsche Bundesbank	1,000	180.0	167.5	652.5
Italy	550	5.0	65.0	480.0
Japan	250	20.0	25.0	205.0
Netherlands	200	40.0	37.5	122.5
Sveriges Riksbank	100	15.0	17.5	67.5
United Kingdom	1,000	—	—	1,000.0
United States	2,000	—	—	2,000.0
Total	6,000	405.0	525.0	5,070.0

TABLE 51. CURRENCIES PURCHASED BY THE FUND WITH GOLD, DECEMBER 1964 AND MAY 1965

(In millions of U.S. dollars)

Members' Currencies	Equivalent of Amount Purchased: Dec. 1964	Equivalent of Amount Purchased: May 1965
Austrian schillings	8.0	—
Belgian francs	17.0	27.5
Canadian dollars	9.0	27.5
Danish kroner	—	5.0
Deutsche mark	93.0	132.5
French francs	63.0	92.5
Italian lire	3.0	32.5
Japanese yen	14.0	22.5
Netherlands guilders	26.0	32.5
Spanish pesetas	10.0	15.0
Swedish kronor	7.0	12.5
Total	250.0	400.0

of each participant in the General Arrangements to Borrow after the completion of the two transactions with the United Kingdom discussed in Chapter 4, and Table 51 the currencies purchased with gold in connection with these transactions.

Table 52 gives details of stand-by arrangements in force during the fiscal year. Some particulars of these arrangements follow.

Brazil

In January 1965, the Fund agreed to a stand-by arrangement with Brazil authorizing purchases equivalent to $125 million; $75 million had been drawn by June 30. The purpose of the arrangement is to support the efforts of the Brazilian authorities to bring about a sharp reduction in

TABLE 52. FUND STAND-BY ARRANGEMENTS WITH MEMBERS, FISCAL YEAR ENDED APRIL 30, 1965

(In millions of U.S. dollars)

Member	Date of Inception	Date of Expiration	Amount	New or Renewed in 1964/65	Amount Available April 30, 1965
Bolivia	Sept. 4, 1963	Sept. 3, 1964 [1]	10.00	—	—
	Sept. 1, 1964	Aug. 31, 1965	12.00	12.00	12.00
Brazil	Jan. 13, 1965	Jan. 12, 1966	125.00	125.00	75.00
Burundi	Jan. 26, 1965	Jan. 25, 1966	4.00	4.00	2.00
Chile	Feb. 14, 1964	Feb. 13, 1965 [2]	25.00	—	—
	Jan. 6, 1965	Jan. 5, 1966	36.00	36.00	24.00
Colombia	Feb. 14, 1964	Feb. 13, 1965	10.00	—	—
Costa Rica	Feb. 1, 1965	Jan. 31, 1966	10.00	10.00	5.00
Dominican Republic	Aug. 1, 1964	July 31, 1965	25.00	25.00	5.00
Ecuador	July 1, 1963	June 30, 1964	6.00	—	—
	July 1, 1964	June 30, 1965	13.00	13.00	10.00
El Salvador	Sept. 13, 1963	Sept. 12, 1964	5.00	—	—
Haiti	Oct. 1, 1963	Sept. 30, 1964	4.00	—	—
	Oct. 1, 1964	Sept. 30, 1965	4.00	4.00	1.75
Honduras	July 18, 1963	July 17, 1964	7.50	—	—
	Aug. 5, 1964	Aug. 4, 1965	7.50	7.50	5.00
India	July 9, 1963	July 8, 1964	100.00	—	—
	Mar. 22, 1965	Mar. 21, 1966	200.00	200.00	75.00
Indonesia	Aug. 1, 1963	July 31, 1964	50.00	—	—
Jamaica	June 13, 1963	June 12, 1964	10.00	—	—
Japan	Mar. 11, 1964	Mar. 10, 1965	305.00	—	—
Korea	Mar. 22, 1965	Mar. 21, 1966	9.30	9.30	9.30
Liberia	June 1, 1963	May 31, 1964	5.70	—	—
	June 1, 1964	May 31, 1965	4.40	4.40	1.10
Mali	July 1, 1964	June 30, 1965	9.90	9.90	—
Nicaragua	Apr. 1, 1964	Mar. 31, 1965	11.25	—	—
Pakistan	Mar. 16, 1965	Mar. 15, 1966	37.50	37.50	37.50
Paraguay	Nov. 23, 1964	Nov. 22, 1965	5.00	5.00	5.00
Peru	Mar. 1, 1964	Feb. 28, 1965	30.00	—	—
	Apr. 8, 1965	Apr. 7, 1966	30.00	30.00	30.00
Philippines	Apr. 12, 1964	Apr. 11, 1965	40.40	—	—
	Apr. 12, 1965	Apr. 11, 1966	40.40	40.40	40.40
Somalia	May 1, 1964	Apr. 30, 1965 [3]	4.70	4.70	—
	Jan. 19, 1965	Jan. 18, 1966	5.60	5.60	3.60
Syrian Arab Republic	Mar. 12, 1964	Dec. 31, 1964	18.50	—	—
Tunisia	Oct. 1, 1964	Sept. 30, 1965	14.25	14.25	3.00
Turkey	Feb. 15, 1964	Dec. 31, 1964	21.50	—	—
	Feb. 1, 1965	Dec. 31, 1965	21.50	21.50	21.50
United Arab Republic	May 23, 1964	May 22, 1965	40.00	40.00	—
United Kingdom	Aug. 8, 1963	Aug. 7, 1964	1,000.00	—	—
	Aug. 8, 1964	Aug. 7, 1965	1,000.00	1,000.00	—
United States	July 22, 1963	July 21, 1964	500.00	—	—
	July 22, 1964	July 21, 1965	500.00	500.00	150.00
Total				2,159.05	516.15

[1] Canceled on August 31, 1964.
[2] Canceled on January 5, 1965.
[3] Canceled on January 18, 1965.

the rate of inflation, to achieve a better balance of external accounts, and to facilitate the country's further economic development, as discussed in Chapter 8.

Burundi

Also in January 1965 a stand-by arrangement for $4 million was agreed with Burundi in conjunction with the establishment of an initial par value for the Burundi franc and the introduction of a comprehensive set of stabilization measures. Under the stand-by arrangement, $2 million was drawn by Burundi in April.

Costa Rica

In conjunction with Costa Rica's acceptance of the obligations of Article VIII, Sections 2, 3, and 4, the Fund agreed in February 1965 to a stand-by arrangement which permits Costa Rica to purchase from the Fund currencies equivalent to $10 million; the equivalent of $5 million had been drawn by June 30. The arrangement was designed to provide additional resources to support the efforts of Costa Rica to maintain financial stability and preserve the convertibility of the colón.

Dominican Republic

A stand-by arrangement with the Dominican Republic for the equivalent of $25 million was introduced in August 1964 to support the Government's policies in the fields of exchange, taxation, and monetary control, aimed at strengthening the country's balance of payments, stabilizing internal costs and prices, bringing about an early settlement of outstanding payment arrears, and restoring full convertibility of the peso. Under the arrangement, $20 million had been drawn by June 30.

India

A stand-by arrangement with India, agreed in March 1965, authorizes purchases of currencies equivalent to $200 million; $150 million had been drawn by June 30. The arrangement was designed to strengthen India's reserve position and support the efforts being made by the authorities to overcome the country's balance of payments difficulties. These efforts include the introduction of higher rates of interest, restraints on the expansion of bank credit, the imposition of a regulatory duty on certain imports, and the adoption of a budget aimed at providing a better balance in the Government's own financial accounts.

Korea

A stand-by arrangement with Korea, also entered into in March 1965, authorizes drawings equivalent to $9.3 million, to reinforce Korea's foreign exchange reserves and support the steps being taken by the Korean authorities to reform the present exchange system and relax restrictions on trade and payments. No drawing under this arrangement was made in the fiscal year.

Mali

A stand-by arrangement with Mali, introduced in July 1964, permits drawings equivalent to $9.9 million and provides support for a comprehensive stabilization program introduced by the Mali authorities. The full amount available under the arrangement has been drawn.

Pakistan

In March 1965 the Fund entered into a stand-by arrangement with Pakistan, authorizing drawings up to a total of $37.5 million. Pakistan's foreign exchange reserves had been declining as a result of a sharp rise in its imports, associated with an import liberalization program and also reflecting a substantial increase in bank credit, especially in the private sector. The stand-by arrangement will assist Pakistan to meet its temporary balance of payments difficulties while taking appropriate steps to restore external equilibrium. Nothing was drawn under this arrangement during the fiscal year.

Paraguay

A stand-by arrangement with Paraguay, agreed in November 1964, authorizes drawings equivalent to $5 million. It is intended to provide support for the country's reserve position in the event of temporary balance of payments difficulties and to assist in the country's efforts to accelerate economic growth in conditions of monetary stability. Paraguay did not find it necessary to draw under the arrangement during the fiscal year.

Somalia

Under its first stand-by arrangement, effective from May 1, 1964, Somalia drew a total of $4.7 million, which was the full amount available. This arrangement was canceled on January 18, 1965 and a new arrangement permitting drawings equivalent to $5.6 million was agreed, effective from January 19, under which the equivalent of $3 million had been drawn by June 30. Both arrangements were in support of a unified and liberal exchange and trade control system being established by Somalia.

Tunisia

The stand-by arrangement with Tunisia, agreed in October 1964, authorizes drawings up to $14.25 million; the equivalent of $11.25 million had been drawn by June 30. The arrangement will support stabilization measures introduced by the Tunisian authorities, aimed at an improvement in the balance of payments and the restoration of financial stability while at the same time allowing a satisfactory rate of growth of the Tunisian economy. These measures accompanied the establishment of a par value which effectively devalued the dinar by some 20 per cent.

United Arab Republic

To provide financial support for the renewed efforts being made by the United Arab Republic to stabilize its economy, the Fund agreed to a stand-by arrangement in May 1964 permitting purchases equivalent to $40 million; the full amount has been drawn.

* * *

In addition to the stand-by arrangements already discussed, arrangements were agreed during the year with Bolivia, Chile, Ecuador, Haiti, Honduras, Liberia, Peru, the Philippines, and Turkey. All were in continuation of the financial support that the Fund had accorded in the preceding year. Those with Bolivia, Chile, and Ecuador replaced arrangements for smaller amounts; those with Haiti, Honduras, Peru, the Philippines, and Turkey replaced arrangements for similar amounts; and that with Liberia replaced a larger one.

The stand-by arrangements agreed during the year were all for a period of one year, except that with Turkey, which was for 11 months.

Any drawing or stand-by arrangement that would increase the Fund's holdings of a member's currency by more than 25 per cent of its quota within any 12-month period (except to the extent that the Fund's holdings of the member's currency are less than 75 per cent of its quota) requires a waiver under Article V, Section 4, of the Articles of Agreement. During the fiscal year, waivers for this purpose were required for all the stand-by arrangements except those with Turkey and the United States. However, no purchases made during the year, other than those under stand-by arrangements, required a waiver.

Repurchases

During 1964/65, 25 members made repurchases equivalent to $517 million (Table 53). Of these members, 12 were in the Western Hemisphere, 4 in Europe, 4 in the Middle East, 4 in Asia, and 1 in Africa. Article V, Section 7(*b*), of the Articles of Agreement provides that a member shall repurchase annually an amount of the Fund's holdings of its currency in excess of 75 per cent of its quota, equivalent to one half of any increase in the Fund's holdings of its currency that has occurred during the Fund's financial year, plus or minus one half of any increase or decrease in its monetary reserves during the same period. Repurchases effected pursuant to Article V, Section 7(*b*), are discussed below (p. 113). Of the repurchases not made pursuant to Article V, Section 7(*b*), most were made on dates when repayments became due, in accordance with schedules to which members had committed themselves, either at the time of their purchases from the Fund or later. Improvements in the monetary reserves positions of several members enabled them to make repurchases before the expiration of the period for which their drawings had been made available, thus

TABLE 53. REPURCHASES OF CURRENCIES FROM THE FUND, FISCAL YEAR ENDED APRIL 30, 1965

(In millions of U.S. dollars)

Members Repurchasing	Amount
Argentina	50.00
Bolivia	2.75
Brazil	44.00
Canada	107.15
Ceylon	3.75
Chile	13.00
Colombia	22.00
Costa Rica	2.07
Ecuador	6.58
Honduras	2.50
India	100.00
Ireland	0.40
Israel	12.49
Italy	65.34
Jamaica	0.24
Jordan	0.30
Malaysia	1.14
Nicaragua	—[1]
Paraguay	0.50
Philippines	11.25
Somalia	0.02
Syrian Arab Republic	2.50
Turkey	16.00
United Arab Republic	18.00
Yugoslavia	35.00
Total[2]	516.97

[1] Less than $5,000.

[2] Total does not equal sum of items because of rounding.

strengthening their secondary line of reserves in the form of potential recourse to the Fund's resources. The drawing by Italy in 1963/64 and the drawing by Canada in 1962/63 have been completely reversed through repurchases by the members and through sales of Italian lire and Canadian dollars by the Fund to other members.

On the other hand, because of balance of payments difficulties, 6 members were unable to meet their repurchase commitments to the Fund when they fell due. The Executive Board agreed to new repurchase schedules for 5 of these members. Under these schedules, repurchases are to be made not later than 5 years from the purchase date. The commitments of 4 members were related to purchases made under stand-by arrangements with undertakings to repurchase within 3 years from the date of purchase. Those of the fifth member related to a purchase under a stand-by arrangement and to another purchase, made initially with a 6-month repurchase commitment, to which postponements had been agreed by the Executive Board on three previous occasions. One member's payment of the repurchase obligation that it had incurred under Article V, Section 7(*b*), as at April 30, 1964 was postponed until July 1965 to coincide with the member's commitment to repurchase in respect of a purchase made under a stand-by arrangement.

In addition, when the Fund's holdings of the currencies of 3 members that had undertaken to repurchase within 3 to 5 years in compliance with the Executive Board Decision on the Use of Fund's Resources and Repurchases, adopted on February 13, 1952,[2] had not been reduced correspondingly after 3 years, these members submitted repurchase schedules providing for repurchases within 5 years from each purchase, and the Fund agreed to these schedules.

Purchases and Repurchases by Currency

Purchases and repurchases during the year ended April 30, 1965 are classified by currency in Table 54, in which the largest drawings, the equivalent of $1,000 million by the United Kingdom and of $475 million by the United States, and repurchases equivalent to $107.15 million by Canada and $65.34 million by Italy are shown separately. Mainly as a result of these transactions, the Fund's holdings of sterling rose to 125.6 per cent of quota on April 30, 1965; its holdings of U.S. dollars rose to 82.8 per cent; its holdings of Canadian dollars were reduced by the equivalent of US$210 million, from 96 per cent to 58 per cent; and its holdings of Italian lire were reduced by the equivalent of $120 million, to 64 per cent of quota. The Fund's holdings of Austrian schillings became proportionately the lowest Fund holdings of any currency, falling, by the equivalent of $25 million, to 3½ per cent of the member's quota by April 30, 1965, and the Fund's holdings of deutsche mark fell by the equivalent of $59.4 million, to 11.4 per cent. During the year there was a net use of the equiva-

[2] Decision No. 102-(52/11); see *Selected Decisions,* pages 21-24.

TABLE 54. DRAWINGS AND REPURCHASES BY CURRENCY, FISCAL YEAR ENDED APRIL 30, 1965

(In millions of U.S. dollars)

	Drawings				Repurchases				
Currency	United Kingdom	United States	Other Countries	Total	Under Article V, Sec. 7(*b*)[1]	Canada	Italy	Other Countries	Total
Gold	—	—	—	—	1.2	—	—	5.5	6.6[2]
Australian pounds	—	—	25.0	25.0	—	—	—	—	—
Austrian schillings	28.0	7.5	9.0	44.5	—	—	3.7	7.8	11.5
Belgian francs	57.0	7.5	12.0	76.5	—	—	3.7	7.8	11.5
Canadian dollars	69.0	25.0	53.0	147.0	—	—	—	20.5	20.5
French francs	163.0	55.0	75.0	293.0	—	—	15.3	63.7	79.0
Deutsche mark	273.0	290.0	53.3	616.3	—	82.2	35.2	166.6	283.9[2]
Italian lire	23.0	25.0	35.3	83.3	—	—	—	20.5	20.5
Japanese yen	54.0	—	20.0	74.0	—	—	—	15.0	15.0
Mexican pesos	—	—	5.0	5.0	—	—	—	—	—
Netherland guilders	66.0	57.5	6.0	129.5	—	25.0	3.7	28.8	57.5
Spanish pesetas[3]	40.0	—	10.0	50.0	—	—	—	—	—
Swedish kronor	27.0	7.5	10.0	44.5	—	—	3.7	3.8	7.5
Pounds sterling	—	—	18.9	18.9	1.8	—	—	1.5	3.3
U.S. dollars	200.0	—	90.0	290.0	0.1	—	—	—	0.1
Total	1,000.0	475.0	422.4[2]	1,897.4[2]	3.1	107.2	65.3	341.4[2]	517.0[2]

[1] Including discharges in respect of previous years.
[2] Total does not equal sum of items because of rounding.
[3] The peseta is not formally convertible and cannot be accepted for repurchases.

lent of $25 million of Australian pounds, $18 million of Belgian francs, $48.6 million of French francs, $25 million of Japanese yen, $5 million of Mexican pesos, $6 million of Netherlands guilders, $40 million of Spanish pesetas, and $15 million of Swedish kronor.

Monetary Reserves and Repurchase Obligations

In accordance with Executive Board Decision No. 1510–(63/23), adopted on May 3, 1963, each member, the amount of whose currency held by the Fund on any April 30 exceeds 75 per cent of its quota, is required to report provisional monetary reserves data to the Fund not later than the following May 31.[3] Furthermore, Rule I-6 of the Fund's Rules and Regulations requires all members to provide final monetary reserves data to the Fund within six months of the end of each financial year of the Fund, i.e., by October 31.

[3] This procedure was confirmed, after review by the Executive Directors, by Decision No. 1813–(65/4), adopted on January 18, 1965 (reproduced in Appendix I, below, and in *Selected Decisions,* p. 53).

On April 30, 1964 the above-mentioned decision applied to 39 members. Repurchase obligations for 10 members were calculated on a provisional basis, and the same 10 members subsequently incurred repurchase obligations calculated on a final basis. Their total amounted to the equivalent of $4,344,368.05, which was payable in gold and convertible currencies, as indicated in Table 55. This table sets out the total net repurchase obligations incurred by members under Article V, Section 7(*b*), since the inception of the Fund. It reflects the fact that Canadian dollars, Salvadoran colones, Guatemalan quetzales, Honduran lempiras, Italian lire, and U.S. dollars could not be accepted by the Fund in discharge of repurchase obligations incurred on April 30, 1964, since on that date the Fund's holdings of each of these currencies were above 75 per cent of the respective member's quota. As a result, an amount equivalent to $20,292,923.73 was abated. Further, repurchase obligations in pounds sterling could be discharged only to the extent that the Fund's holdings of that currency on April 30, 1964 were below 75 per cent of the U.K. quota;

TABLE 55. REPURCHASE OBLIGATIONS UNDER ARTICLE V, SECTION 7(*b*), OF THE FUND AGREEMENT, AT APRIL 30, 1948-64

(In thousands of U.S. dollars)

	Number of Members Affected	Total Amount	Gold	U.S. Dollars	Pounds Sterling	Canadian Dollars	Deutsche Mark	French Francs	Other Currencies
1948	3	7,336	929	6,407	—	—	—	—	—
1949	4	27,299	9,439	17,861	—	—	—	—	—
1950	6	47,594	21,156	26.438	—	—	—	—	—
1951	7	68,608	19,125	49,483	—	—	—	—	—
1952	4	39,182	38,340	842	—	—	—	—	—
1953	5	84,484	35,554	48,920	—	10	—	—	—
1954	10	80,525	34,440	46,084	—	—	—	—	—
1955	7	195,794	68,222	127,554	—	18	—	—	—
1956	10	32,581	11,118	21,450	—	13	—	—	—
1957	8	104,010	38,228	65,775	—	3	—	—	5
1958	7	238,975	90,998	147,848	—	124	—	—	5
1959	8	308,754	142,994	165,711	—	48	—	—	—
1960	8	201,550	124,968	76,192	—	379	—	—	11
1961	8	68,310	53,633	14,366	—	298	—	—	13
1962	10	81,645	18,857	61,341	—	7	1,330	3	106 [1]
1963	17	97,052	27,242	62,615	7,011	—	73	106	6
1964	10	4,344	1,850	—	1,627	—	318	14	536 [2]
		1,688,043	737,093	938,887	8,638	900	1,721	123	682

[1] Includes the equivalent of $22,000 in Italian lire, $49,000 in Netherlands guilders, and $28,000 in Swedish kronor.

[2] Includes the equivalent of $56,000 in Austrian schillings, $148,000 in Belgian francs, and $332,000 in Netherlands guilders.

of the repurchase obligations that accrued in this currency an amount equivalent to $1,140,702.68 was abated. Simultaneously, the limitation on repurchase obligations imposed by Article V, Section 7(*c*)(i), which provides that repurchases shall not be carried to a point at which the repurchasing member's monetary reserves are below its quota, has become applicable to a wider extent as members' quotas have been increased. Of the total gross repurchase obligations at April 30, 1964, calculated on a final basis, no less than 83 per cent was abated.

At the end of October 1964, a total of 32 members had not submitted monetary reserves data. Most of these were new Fund members in the process of establishing reporting systems to collect the information necessary to comply with the Fund's requirements. By the end of April 1965, data from 9 members were still outstanding. None of these members could have incurred a repurchase obligation at April 30, 1964, as the currencies of 8 members were not held by the Fund on that date, and the Fund's holdings of the ninth member's currency were below 75 per cent of the member's quota.

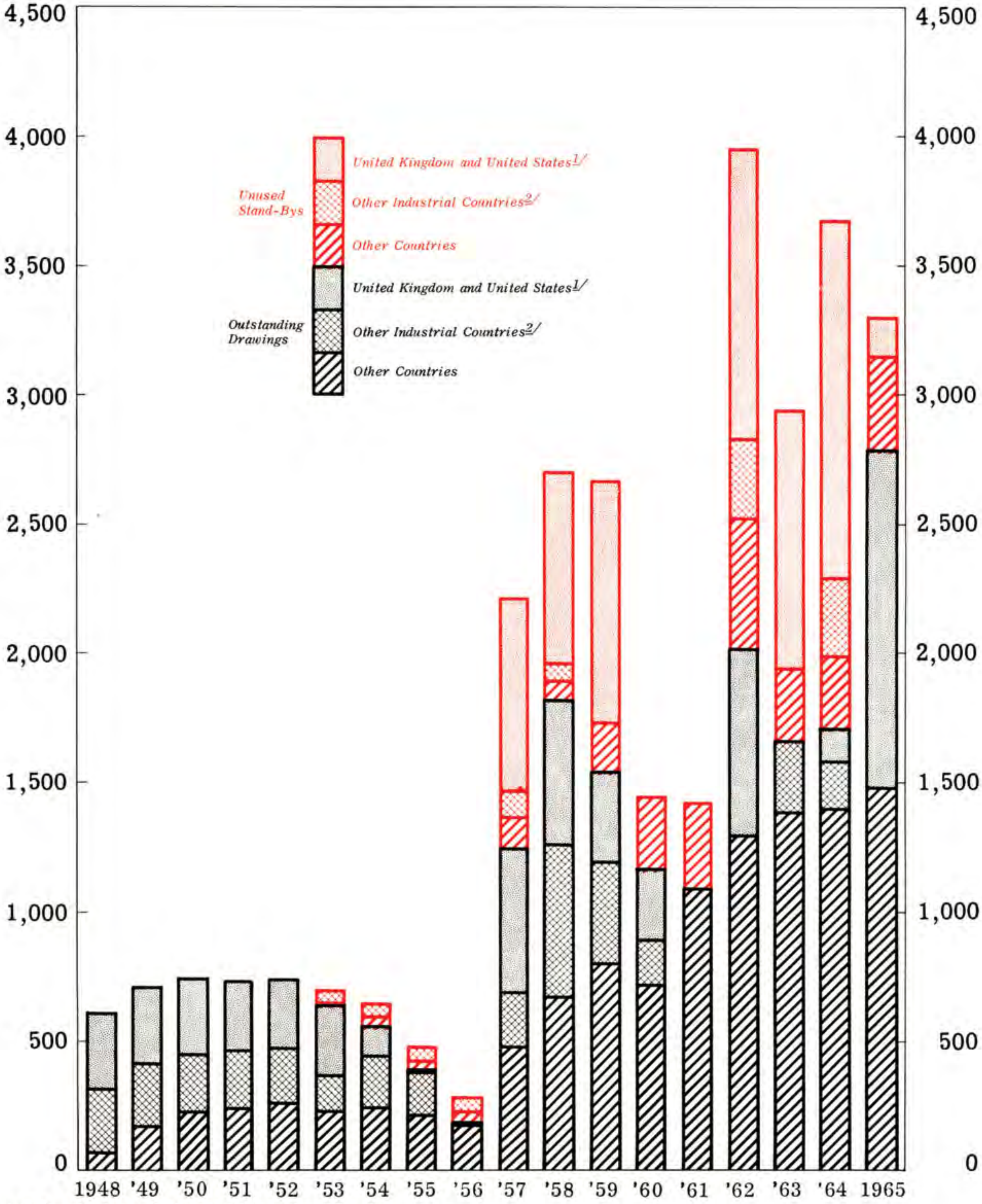
Summary of Transactions, 1948-65

Between the inception of Fund operations and April 30, 1965, 58 members purchased currency from the Fund and 3 other members had stand-by arrangements without drawing under them. Of these 61 members, 20 were in Central and South America, 14 in Europe, 9 in Africa, 8 in the Far East and Western Pacific, 7 in the Middle East, and 3 in North America. Total sales by the Fund were equivalent to $9.37 billion. The transactions are summarized in Table 56. Drawings outstanding at April 30 in each year, together with the amounts available (but not used) under stand-by arrangements on the same date, are shown in Chart 30.

By April 30, 1965, drawings made by 47 members had been wholly or partly reversed, either through repurchases in gold or convertible currencies or as a result of purchases of their

CHART 30. OUTSTANDING BALANCES OF DRAWINGS FROM THE FUND, AND UNUSED STAND-BY ARRANGEMENTS, ON APRIL 30, 1948-65

(In millions of U.S. dollars)



[1] United States included in 1964 and 1965 only.
[2] Belgium, Canada, Denmark, France, Italy, Japan, Netherlands, and Norway.

TABLE 56. SUMMARY OF FUND TRANSACTIONS, FISCAL YEARS ENDED APRIL 30, 1948-65

(In millions of U.S. dollars)

	Total Purchases by Members	Total Stand-By Arrangements in Force at End of Fiscal Year	Total Repurchases by Members
1948	606.04	—	—
1949	119.44	—	—
1950	51.80	—	24.21
1951	28.00	—	19.09
1952	46.25	—	36.58
1953	66.12	53.00	184.96
1954	231.29	90.00	145.11
1955	48,75	90.00	276.28
1956	38.75	97.50	271.66
1957	1,114.05	968.90	75.04
1958	665.73	884.28	86.81
1959	263.52	1,132.84	537.32
1960	165.53	291.88	522.41
1961	577.00	338.62	658.60
1962	2,243.20	1,942.88	1,260.00
1963	579.97	1,287.25	807.25
1964	625.90	1,970.15	380.41
1965	1,897.44	516.15	516.97
Total [1]	9,368.78		5,802.68 [2]

[1] Totals may not equal sums of items because of rounding.

[2] Including $281.6 million repurchased in excess of drawings. Of this amount, $257.5 million represents repurchases that reduced the Fund's holdings of members' currencies below the amounts originally paid on subscription account, and $24.1 million represents repurchases of members' currencies paid as charges. Repurchases do not include sales of currencies equivalent to $1,067.2 million offset by adjustments of $8.7 million, making a net total of $1,058.5 million having the effect of repayment.

currencies by other members. On that date the total amount of members' purchases still outstanding was equivalent to US$2,789.3 million: the amounts drawn had been outstanding for the following periods:

	Amount in millions of U.S. dollars	Number of members involved
12 months or less	1,725.7	28
13 to 18 months	46.2	8
19 to 24 months	214.0	13
25 to 30 months	104.9	10
31 to 36 months	162.8	11
37 to 42 months	88.7	5
43 to 48 months	349.3	7
49 to 54 months	73.2	6
55 to 60 months	24.5	3

Fund Charges

Currently, 26 members are paying the charges levied by the Fund on its holdings of members' currencies in excess of their quotas; the amount of such charges incurred during the year totaled $35.9 million, compared with $31.5 million during the preceding year. Since the beginning of the Fund's operations, 48 members have been subject to such charges. At present, part of these charges is paid by 4 members in their own currencies, in accordance with Article V, Section 8(*f*), of the Fund Agreement, which permits such payments if a member's monetary reserves are less than half of its quota. The present schedule of charges to be levied on the Fund's holdings of a member's currency in excess of quota, which has been in effect from May 1, 1963, was reviewed by the Executive Board and extended until April 30, 1966. The schedule is reproduced in each issue of *International Financial Statistics.* Service charges on drawings totaled $9.5 million during the year under review, compared with $3.1 million in 1963/64. Charges collected on stand-by arrangements, after deduction of the amounts credited against service charges if and when drawings were made under the arrangements, and of refunds resulting from changes in the level of the Fund's holdings of members' currencies that re-created or increased the member's gold tranche, totaled $0.9 million during the year ended April 30, 1965. These charges are not considered as income until the expiration or cancellation of the stand-by arrangement; the income derived from them in the past fiscal year was $2.1 million. Charges paid by the Fund in accordance with paragraph 9(a) of the General Arrangements to Borrow amounted to $2 million, and interest paid by the Fund in accordance with paragraph 9(b) amounted to a total of $2.5 million. Both charges and interest were paid in gold.

Consultations with Members

Member countries that are availing themselves of transitional arrangements in accordance with Article XIV, Section 2, of the Fund Agreement are required by that Article to consult with the Fund annually on the retention of their exchange restrictions. These consultations have continued to provide opportunities for the examination of the economic and financial problems that have given rise to restrictive and discriminatory practices, and the Fund has again continued its endeavors to help in the elimination of such practices. Several of the consultations under Article XIV have been combined with discussions of new financial programs or have included reviews of such programs already being implemented. During the fiscal year 1964/65, consultations under Article XIV were concluded with 43 countries; with others, the procedure had been initiated but had not been completed by the end of the fiscal year.

Consultations were also held with 22 members that have accepted the obligations of Article VIII, Sections 2, 3, and 4, of the Fund Agreement. Consultations with one Article VIII country were still in progress at the end of the fiscal year. The Executive Board Decision No. 1034–(60/27) of June 1, 1960 [4] stressed the merit of holding periodic discussions between the Fund and its members even if no question involving action under Article VIII should arise. These discussions include exchanges of views on monetary and fiscal developments and enable the Fund to further the objective of securing the fullest possible degree of consultation and collaboration on international monetary problems.

Relations with Other International Organizations

As in previous years, many of the organizations which have responsibilities in fields related to the Fund's, and with which the Fund maintains particularly close contacts—the United Nations (UN), the CONTRACTING PARTIES to the General Agreement on Tariffs and Trade (GATT), the Organization for Economic Cooperation and Development (OECD), the Bank for International Settlements (BIS), and the Inter-American Development Bank (IDB)—were represented at the joint Annual Meetings in Tokyo of the Fund and the International Bank for Reconstruction and Development (IBRD), with which the Fund has a special relationship. During the fiscal year, Fund representatives attended meetings of these organizations and continued direct working relationships with their staffs.

The Managing Director of the Fund addressed the 38th Session of the UN Economic and Social Council (ECOSOC), at which the Annual Report of the Fund was presented. Fund representatives attended, among other UN meetings, the 19th Session of the General Assembly, the 37th and 38th Sessions of ECOSOC, the 13th and 14th Sessions of the Governing Council of the Special Fund, meetings of the Economic Commissions for Africa, Asia and the Far East, Europe, and Latin America, and the 1st Session of the newly created UN Trade and Development Board. The Managing Director and the Deputy Managing Director attended meetings of the UN Administrative Committee on Coordination, and Fund representatives participated in meetings of its Preparatory Committee and subsidiary Consultative Committees. Members of the staff participated in meetings of the UN Inter-Regional Workshop on Problems of Budget Classification and Management in Copenhagen, the Inter-Agency Meeting on Selected Management Problems in Paris, and the Conference of European Statisticians' Working Group on National Accounts and Balances in Geneva. In the area of commodities, a Fund representative attended the International Tin Conference in New York and meetings in Washington of the International Rubber Study Group's Management Committee and the International Cotton Advisory Commitee.

The Fund, in cooperation with the IBRD, assisted the UN Economic Commission for Africa in making arrangements for, and was represented at, a meeting of African monetary authorities in Tokyo, held after the joint Annual Meetings, and Fund representatives attended the inaugural meeting of the African Development Bank in Lagos.

Following the extension of existing arrangements for cooperation with the OECD, Fund representatives have attended meetings of its Economic Policy Committee's Working Party 3, which is concerned with policies for the promotion of better international payments equilibrium.

[4] *Selected Decisions,* pages 81-83.

The Managing Director and other Fund representatives attended meetings of the BIS in Basle.

In Latin America, Fund representatives attended the third annual meetings in Lima of the Organization of American States (OAS) Inter-American Economic and Social Council at the Expert and Ministerial Levels, the sixth annual meeting of the Board of Governors of the IDB in Asunción, and the first Regional Meeting of Latin American Bankers in Mar del Plata, Argentina; participated informally in an advisory capacity in a series of meetings of the Inter-American Committee on the Alliance for Progress (CIAP) held in Washington; and participated in the eighth operational meeting of the Latin American Center for Monetary Studies (CEMLA) in Caracas.

A Fund staff member attended the 51st Conference of the International Law Association in Tokyo.

Fund representatives have attended sessions and other meetings of the CONTRACTING PARTIES to the GATT in Geneva. The CONTRACTING PARTIES consulted the Fund in connection with their consideration of import restrictions maintained by individual countries for balance of payments reasons, as well as in other connections where balance of payments or exchange matters were involved. The Fund transmitted to the CONTRACTING PARTIES the decisions and background material resulting from its own consultations with various governments consulting under the balance of payments provisions of the GATT; Fund representatives cooperated with the Committee on Balance of Payments Restrictions and with other GATT bodies dealing with related matters.

Staff

At the end of the fiscal year, the Fund staff numbered 674, including 19 temporary employees and 1 on extended leave. This total represents a net increase of 79 over the total at the beginning of the year. During the year, 153 new staff members were appointed from 42 member countries. Nationals of 64 countries are now on the staff.

The Exchange Restrictions Department has been reorganized and renamed the Exchange and Trade Relations Department, in consideration of a number of changes in its role and responsibilities. It will continue to work in the field of exchange restrictions and multiple currency practices. In addition, it will study and evaluate the Fund's activities with regard to exchange reforms, stabilization policies, and stand-by arrangements and will be concerned with a number of other matters, including regional payments arrangements and debt renegotiations. The Department will be primarily responsible for the Fund's collaboration with the GATT and with the United Nations Conference on Trade and Development (UNCTAD), which was established in January 1965 as an organ of the UN General Assembly.

Publications

The Fund's regular program of publications was continued in 1964-65: *Annual Report of the Executive Directors for the Fiscal Year Ended April 30, 1964* (Nineteenth Annual Report), with shortened versions in French, German, and Spanish; *Balance of Payments Yearbook,* Volume 16, 1959-63; *Fifteenth Annual Report on Exchange Restrictions; International Financial News Survey,* weekly; *International Financial Statistics,* monthly, *Supplement to 1964/65 Issues,* and *Supplement on Money; Schedule of Par Values,* 38th and 39th issues; *Staff Papers,* Volume XI, Nos. 2 and 3, and Volume XII, No. 1; and *Summary Proceedings of the Nineteenth Annual Meeting of the Board of Governors.*

In conjunction with the International Bank for Reconstruction and Development, the Fund published *Direction of Trade,* monthly, and *Finance and Development,* quarterly (English, French, and Spanish editions).

Other publications of the Fund in 1964-65 were *Selected Decisions of the Executive Directors and Selected Documents* (third issue, January 1965—previously entitled *Selected Decisions of the Executive Directors*) and four pamphlets descriptive of the Fund's activities: *Introduction to the Fund; The International Monetary Fund: Its Form and Functions; The International Monetary Fund and Private Business Transactions: Some Legal Effects of the Articles of Agreement;*

and *The International Monetary Fund and International Law: An Introduction.* All these pamphlets have been published in English and some in French and Spanish; French and Spanish translations of the others are in preparation.

All the above are available without charge except for the *Balance of Payments Yearbook, International Financial Statistics* (and Supplements), *Staff Papers,* and *Direction of Trade,* which are available by subscription. Hitherto these publications have cost a total of $33.50 a year to general subscribers and $30.50 a year to universities; they have now been made available to university libraries, faculties, and students at the special rate of $3 a year for any one of them or $10 a year for all four.

Administrative Finance

During the financial year, the Fund's operating income, equivalent to $47.7 million, exceeded its total expenditure by $25.5 million. This amount was transferred provisionally to the General Reserve pending action by the Board of Governors. The General Reserve now totals the equivalent of $141.8 million.

The Fund continued to invest a part of its gold holdings in U.S. Government securities, with the understanding that the same quantity of gold can be reacquired whenever the investment is terminated. The amount so invested was $800 million. The income therefrom amounted to $30.75 million for the financial year; it was credited to a Special Reserve, which showed a balance of $148.3 million on April 30, 1965.

The administrative budget approved by the Executive Directors for the period May 1, 1965–April 30, 1966 is presented in Appendix IV. Comparative income and expenditure figures for the fiscal years ended 1963, 1964, and 1965 are given in Appendix V.

The Executive Board requested the Governments of El Salvador, Thailand, and the United Kingdom to nominate members of the Audit Committee for 1965. The following nominations were made and confirmed: Mr. Juan Samuel Quinteros, Superintendent, Superintendency of Banks and Other Financial Institutions, Central Bank of El Salvador; Mr. Panas Simasathien, Chief of Accounting and Fiscal Systems Division, Comptroller General's Department, Ministry of Finance, Thailand; Mr. Ronald William Tizard, Deputy Director of Audit, Exchequer and Audit Department, United Kingdom. The report of the Committee is submitted separately. Appendix VI gives the Auditors' Certificate, together with the audited Balance Sheet as at April 30, 1965 and the audited Statement of Income and Expenditure for the financial year.

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APPENDICES

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Appendix I. Executive Board Decisions and Report to Board of Governors

A. Calculation of Repurchase Obligations: Prompt Reporting of Monetary Reserves Data

1. Where on any April 30 the Fund holds a member's currency in an amount exceeding 75 per cent of the member's quota, the member shall make a provisional monetary reserves report to the Fund not later than May 31, preferably by cable.

2. The Fund will make a provisional calculation of the amount and distribution of the repurchase obligations of such members and will inform them of the results of the calculation not later than June 15. Members shall discharge within thirty days any repurchase obligations as thus provisionally calculated and agreed with the member.

3. All provisional repurchases shall be subject to adjustment by members and the Fund in accordance with Rule I–6 of the Fund's Rules and Regulations.

Decision No. 1813–(65/4)

January 18, 1965

B. Procedure for Drawings in the Gold Tranche

When a duly authenticated request to draw in the gold tranche is received from a member, the request shall be notified to the Executive Board on the day it is received, whenever possible, or on the next business day, and unless, by the close of that business day, the Managing Director decides or an Executive Director requests that the matter be placed on the Board's agenda for discussion, the Fund shall, at the close of the first business day following the date of the receipt of the request, instruct the appropriate depository to make the transfer on the next business day after the instruction or as soon as possible thereafter.

Decision No. 1745–(64/46)

August 3, 1964

C. Increases in Quotas of Members—Fourth Quinquennial Review

Report of the Executive Directors to the Board of Governors

1. At its Nineteenth Annual Meeting in Tokyo, the Board of Governors adopted the following Resolution:

RESOLVED:

That the Executive Directors proceed to consider the question of adjusting the quotas of members of the Fund and at an early date submit an appropriate proposal to the Board of Governors.

2. Pursuant to this Resolution, the Executive Directors have considered the question of adjusting the quotas of members and have concluded that in a world in which income and trade have expanded rapidly and are expected to do so, the need for the type of liquidity provided by the Fund, like the need for international liquidity in general, may be expected to grow. A reasonable expansion in quotas would increase the Fund's resources relative to the calls that are likely to be made upon them and enhance confidence in the Fund's ability to meet all justifiable requests for drawings. Provision of adequate resources, enabling the Fund to meet needs with a greater margin of safety, may also reduce those needs by marshaling the resources and demonstrating the international cooperation that could deter speculation. Accordingly, the Executive Directors have decided that proposals for increases in present quotas of 25 per cent, subject to the appropriate rounding of the resulting figures, and for larger increases for certain members should be submitted to the Board of Governors. For the purposes of this Report, present quotas are quotas as of February 26, 1965 or the maximum amount to which quotas could be increased under Resolutions adopted by or submitted to the Board of Governors before that date. The general increases of 25 per cent are provided for by the First of two Resolutions submitted to the Board of Governors with this Report. The formula for rounding the increased quotas is as follows: amounts below $500 million are rounded to the next higher multiple of one million, and amounts of $500 million or more are rounded to the next higher multiple of five million. The quotas to which members can consent under the First Resolution are shown in the Annex to this Report. The Second Resolution submitted with this Report provides for the special (i.e., larger) increases. If the Board of Governors agrees to propose a special increase for a member under the Second Resolution, the member will be able to consent to that increase or to the smaller increase under the First Resolution. When such a member consents, it should declare under which Resolution it is choosing to consent, and its choice will then be final.

3. The increases in quotas under the attached Resolutions are without prejudice to the adjustment of quotas that members can request under the Fund's Decision on "Compensatory Financing of Export Fluctuations" (E.B. Decision No. 1477–(63/8), February 27, 1963). In this connection, E.B. Decision No. 1529–(63/33), June 14, 1963 will continue to be applicable.

4. The attached Resolutions are designed to enable the Board of Governors to vote at one time on all matters connected with the increases in quotas under the two Resolutions. Governors are requested to vote on both Resolutions. The First Resolution is to

be voted on as a whole. In the case of the Second Resolution, Governors may vote on all or each of the special increases. Under the Resolutions, it will be possible for increases in quotas to become effective without the need for further reference to the Board of Governors. Attention is drawn to the requirement that, to be valid, votes must be received at the seat of the Fund on or before March 31, 1965.

5. If the Resolutions are adopted by the necessary majority of four-fifths of the total voting power, as required by Article III, Section 2 of the Articles of Agreement, a member may consent to the increase in its quota at any time on or before September 25, 1965. Therefore, unless this period is extended by the Executive Directors, members will have until September 25, 1965 to take whatever action may be necessary under their laws to enable them to give their consent.

6. In view of the cooperative nature of the increase in quotas under the Resolutions, it is provided that increases will not become effective until the Fund has determined that members having two-thirds of the total of quotas on February 26, 1965 have consented to increases in their quotas. In determining whether this degree of participation has been reached, the Fund will take into account all consents to increases, whether they be under the First or Second Resolutions and whether they be increases in full or by installments.

7. In view of past practice, any member consenting to a special increase under the Second Resolution will be expected to request an increase in its subscription to the capital of the International Bank for Reconstruction and Development corresponding to the special part of the increase in quota.

8. Under the Resolutions, a member may pay its additional subscription in respect of the increase in its quota at any time before it is due. If a member pays before the increase in its quota takes effect, the additional subscription will be kept in separate accounts of the Fund and returned if it should be established that the increase cannot take effect. A member is required to pay its additional subscription not later than 30 days after the later of the following events: (i) its consent to its quota increase, and (ii) the determination by the Fund, referred to in paragraph 6 above, that the condition as to participation in quota increases has been satisfied.

9. Increases in members' quotas will take effect as follows:

(a) When a member pays its additional subscription before the later of the two events referred to in the preceding paragraph, the increase in its quota will take effect on the happening of the later of these events.

(b) If a member pays its additional subscription after the later of these two events, the increase in its quota will take effect on the day of payment.

10. Each member increasing its quota must pay an additional subscription equal to the increase, of which 25 per cent shall be in gold and the balance in its currency. Payment of both portions of the additional subscription must be made before the increase in the member's quota can become effective, even by those members which, in accordance with the Articles of Agreement or Membership Resolutions, have not yet been required to pay their original subscriptions.

11. The increase in quotas under the Resolutions is based on the idea of a cooperative effort by the members of the Fund to provide larger resources against contingencies that may affect any member. In order to preserve the general character of that effort, it has been thought preferable not to exercise the discretion given to the Executive Directors under Article III, Section 4 of the Articles of Agreement to reduce gold payments in connection with these Resolutions. However, the payment in gold of 25 per cent of the quota increase may cause hardship in some cases, and therefore the Executive Directors have decided that the policies and practices described in the following paragraphs of this Report will be applied.

12. Under the Resolutions any member consenting to an increase in its quota may consent to an increase by installments. Each installment of the increase would correspond to the amount of additional subscription in gold and currency paid by the member. Any member consenting to an increase by installments must pay an original installment of additional subscription, and an installment in each period of 12 months thereafter. Each installment shall be one-fifth of the increase. Members may accelerate payment under this installment schedule.

13. A member that wishes to have the full increase in its quota take effect immediately or to expedite the full increase in its quota if it is paying under the installment schedule may find it a hardship to make prompt payment in gold of 25 per cent of the increase in its quota. In order to alleviate this hardship the member may request an exchange transaction in accordance with paragraphs 14 through 19 below.

14. Where a member requests an exchange transaction within the gold tranche, the established gold tranche policy and procedure will apply.

15. A member consenting to an increase in its quota under the First Resolution may request an exchange transaction beyond the gold tranche in an amount not in excess of 25 per cent of the increase. This facility will be available where (a) the member represents that it would encounter undue payments difficulties through the reduction in its reserves by the payment of the 25 per cent gold subscription or of the outstanding balance of that subscription; and (b) the member requests the exchange transaction within six months after the date of the consent to the increase or the determination by the Fund that the condition as to participation in quota increases has been satisfied, whichever is later.

16. The Fund will expect that a member requesting an exchange transaction under paragraph 15 above will represent that it will make a repurchase corresponding to the exchange transaction in accordance with the principles of E.B. Decision No. 102–(52/11) of February 13, 1952 and the following sub-paragraphs:

(i) The member will be expected to represent that it will make a repurchase corresponding to the exchange transaction in equal annual installments, to commence one year after the transaction and to be completed not later than five years after the transaction.

(ii) If the member, when requesting the exchange transaction or at any time thereafter, represents that, because of other repurchase commitments or for such other reasons as it shall submit, the schedule referred to in (i) above would create undue payments difficulties, the Fund may accept a representation that the member will repurchase in accordance with the provisions of E.B. Decision No. 102–(52/11).

17. The representation of a member with respect to undue payments difficulties referred to in paragraphs 15 and 16 above would not be challenged by the Fund except where it was clearly evident that the representation was without basis.

18. In order to facilitate the exchange transactions referred to in paragraph 15 above, the Fund will be prepared, where necessary, to grant a waiver of the quantitative limits prescribed in Article V, Section 3(*a*)(iii) of the Articles of Agreement. The Fund will also be prepared to grant such a waiver, in appropriate cases, to the extent that an exchange transaction in accordance with the preceding paragraphs is still outstanding.

19. A member requesting an exchange transaction in accordance with the preceding paragraphs will be expected to consult the Managing Director on the currency to be drawn under E.B. Decision No. 1371–(62/36) of July 20, 1962. Many such members are likely to use the currency drawn to purchase gold from the monetary authorities of the member whose currency was drawn either to pay their additional gold subscription or to restore the level of their gold holdings if they have already paid the additional subscription. Normally, these members would purchase the gold from a reserve currency member. With a view to alleviating the impact on the gold holdings of the reserve currency members that would result from such purchases, the Fund, in the course of the consultation on the currency to be drawn, will suggest that certain of these exchange transactions, up to the equivalent of $150 million, be made in currencies which the Fund would then replenish by the sale of gold under Article VII, Section 2(ii) up to the amount of such transactions.

20. The exchange transactions and replenishment of currency referred to in the preceding paragraphs will partially alleviate the impact of the additional gold subscriptions of members on the gold holdings of the reserve currency members. However, it is expected that, notwithstanding this alleviation and the likelihood that many members will meet their additional gold subscription from their own gold holdings, other members will purchase a substantial amount of gold from the reserve currency members, and in particular the United States and the United Kingdom. In order to provide a measure of further alleviation solely in connection with the quota increases provided for by the Resolutions submitted with this Report, the Fund will make general deposits of gold with its gold depositories designated by the United States and the United Kingdom in a total amount not exceeding the equivalent of $350 million. Approximately $250 million in gold will be placed on general deposit with the Fund's depository in the United States and approximately $100 million with the Fund's depository in the United Kingdom. Within the limit of $350 million or the reduced amount under paragraph 21 below, adjustments may be made in the amounts held on general deposit in these two depositories on the basis of the actual impact on the gold holdings of each of the two members of the sales of gold by them in connection with the additional subscriptions of other members.

21. If the Fund determines that the total sales of gold by the United States and the United Kingdom in connection with the additional subscriptions of other members are less than the equivalent of $350 million, the Fund will reduce its general deposits accordingly.

22. The general deposits will be subject to the following principles:

(a) A general deposit of gold by the Fund shall be a demand deposit. Accordingly, the Fund shall be entitled, at its sole discretion and on its demand to the depository, to the immediate transfer to an earmarked account in the sole name of the Fund at the depository, free of any claims, liens or encumbrances in favor of any other party, of an amount of gold not in excess of the amount then held by the Fund on general deposit with the depository, which transfer shall be made without charge or cost to the Fund.

(b) Whenever a member that designated the depository with which a general deposit is held so requests, the Fund shall demand that the depository transfer gold in the amount requested to an earmarked account.

(c) On the occasion of any use of gold, the Fund would normally use, in appropriate proportions, earmarked gold and gold on general deposit in accordance with the good management of its assets.

(d) The Managing Director will report periodically to the Executive Directors on the Fund's general deposits, and the Executive Directors shall review the policy with respect to general deposits not later than five years after the first such deposit is made.

February 26, 1965

Annex to Report

	Present Quota[1] (Million U.S. dollars)	Increased Quota Under First Resolution (Million U.S. dollars)
1. Afghanistan	22.50	29
2. Algeria	60.00	75
3. Argentina	280.00	350
4. Australia	400.00	500
5. Austria	75.00	94
6. Belgium	337.50	422
7. Bolivia	22.50	29
8. Brazil	280.00	350
9. Burma	30.00	38
10. Burundi	11.25	15
11. Cameroon	15.00	19
12. Canada	550.00	690
13. Central African Republic	7.50	10
14. Ceylon	62.00	78
15. Chad	7.50	10
16. Chile	100.00	125
17. China	550.00	690
18. Colombia	100.00	125
19. Congo (Brazzaville)	7.50	10
20. Congo, Democratic Republic of	45.00	57
21. Costa Rica	20.00	25
22. Cyprus	11.25	15
23. Dahomey	7.50	10
24. Denmark	130.00	163
25. Dominican Republic	25.00	32
26. Ecuador	20.00	25
27. El Salvador	20.00	25
28. Ethiopia	15.00	19
29. Finland	57.00	72
30. France	787.50	985
31. Gabon	7.50	10
32. Germany, Federal Republic of	787.50	985
33. Ghana	55.00	69
34. Greece	60.00	75
35. Guatemala	20.00	25
36. Guinea	15.00	19
37. Haiti	11.25	15
38. Honduras	15.00	19
39. Iceland	11.25	15
40. India	600.00	750
41. Indonesia	165.00	207
42. Iran	70.00	88
43. Iraq	55.00	69
44. Ireland	45.00	57
45. Israel	50.00	63
46. Italy	500.00	625
47. Ivory Coast	15.00	19
48. Jamaica	20.00	25
49. Japan	500.00	625
50. Jordan	11.25	15
51. Kenya	25.00	32
52. Korea	18.75	24
53. Kuwait	50.00	63
54. Laos	7.50	10
55. Lebanon	6.75	9
56. Liberia	.11.25	15
57. Libya	15.00	19
58. Luxembourg	15.00	19
59. Malagasy Republic	15.00	19
60. Malaysia	100.00	125
61. Mali	13.00	17
62. Mauritania	7.50	10
63. Mexico	180.00	225
64. Morocco	52.50	66
65. Nepal	7.50	10
66. Netherlands	412.50	520
67. New Zealand	125.00	157
68. Nicaragua	11.25	15
69. Niger	7.50	10
70. Nigeria	50.00	63
71. Norway	100.00	125
72. Pakistan	150.00	188
73. Panama	11.25	15
74. Paraguay	11.25	15
75. Peru	37.50	47
76. Philippines	75.00	94
77. Portugal	60.00	75
78. Rwanda	11.25	15
79. Saudi Arabia	72.00	90
80. Senegal	25.00	32
81. Sierra Leone	11.25	15
82. Somalia	11.25	15
83. South Africa	150.00	188
84. Spain	150.00	188
85. Sudan	45.00	57
86. Sweden	150.00	188
87. Syrian Arab Republic	30.00	38
88. Tanzania	25.00	32
89. Thailand	76.00	95
90. Togo	11.25	15
91. Trinidad and Tobago	20.00	25
92. Tunisia	22.50	29
93. Turkey	86.00	108
94. Uganda	25.00	32
95. United Arab Republic	120.00	150
96. United Kingdom	1,950.00	2,440
97. United States	4,125.00	5,160
98. Upper Volta	7.50	10
99. Uruguay	30.00	38
100. Venezuela	150.00	188
101. Viet-Nam	22.50	29
102. Yugoslavia	120.00	150

[1] As defined in paragraph 2 of the Report and paragraph 1(a) of the First Resolution.

Resolutions Submitted to the Board of Governors

WHEREAS the Executive Directors have considered the question referred to them by the Resolution of the Board of Governors of the International Monetary Fund at its Nineteenth Annual Meeting:

> "That the Executive Directors proceed to consider the question of adjusting the quotas of members of the Fund and at an early date submit an appropriate proposal to the Board of Governors."

Have found that proposals to carry out increases in quotas should be submitted to the Board of Governors; and

Have submitted to the Board of Governors a Report entitled "Increases in Quotas of Members—Fourth Quinquennial Review" and the following Resolutions of the Board of Governors for a vote without meeting pursuant to Section 13 of the By-Laws of the Fund, which Resolutions propose increases in the quotas of all members of the Fund, make provision for consents by members, and establish the conditions upon which the increases shall take effect;

Now, THEREFORE, the Board of Governors, noting the said Report of the Executive Directors, hereby resolves that:

First Resolution

1. (a) The International Monetary Fund proposes that, subject to the provisions of this First Resolution, the quotas of all members of the International Monetary Fund in effect on February 26, 1965 or the maximum quotas to which members could consent under Resolutions adopted by or submitted to the Board of Governors before that date shall be increased by 25 per cent, with the resulting amounts rounded according to the following formula:

    amounts below $500 million shall be rounded to the next higher multiple of one million;

    amounts of $500 million or more shall be rounded to the next higher multiple of five million.

   (b) When an increase in quota proposed in this First Resolution is calculated on the basis of a quota that includes an increase to which a member can consent under another Resolution adopted by or submitted to the Board of Governors before February 26, 1965 and there is no consent to such increase, the increase proposed in this First Resolution shall be 25 per cent of the quota in effect on February 26, 1965, rounded in accordance with paragraph 1(a).

2. None of the increases in quotas proposed in this First Resolution shall become effective unless:

   (i) The member concerned has notified the Fund that it consents to the increase in its quota; and

   (ii) The Fund determines that members having not less than two-thirds of the total of quotas on February 26, 1965 have consented to increases in their quotas under the First or Second Resolution; and

   (iii) The member concerned has paid the full increase in its quota.

   Subject to paragraph 6(c), each increase in quota shall become effective upon the date of the latest of these three events.

3. Notices in accordance with paragraph 2(i) shall be executed by a duly authorized official of the member.

4. Notices in accordance with paragraph 2(i) shall be received in the Fund not later than September 25, 1965, provided that the Executive Directors may extend this period as they may determine.

5. Subject to paragraph 6(b), each member shall pay to the Fund within 30 days after the later of the two events in paragraph 2(i) and (ii), 25 per cent of the increase in gold and the balance in its own currency.

6. (a) In giving notice in accordance with paragraph 2(i), any member may consent to the increase in its quota as an increase by installments.

   (b) Notwithstanding paragraph 2(iii), a member increasing its quota by installments shall pay not less than one-fifth of the gold and currency prescribed in paragraph 5 within 30 days after the later of the two events in paragraph 2(i) and (ii) and shall pay further installments of gold and currency of not less than one-fifth of the increase in each twelve months after the first payment until the full amount prescribed in paragraph 5 has been paid.

   (c) Subject to paragraph 2, on the completion of the payment of each installment of the increase, the member's quota shall be increased by an amount equal to the installment.

7. Since it is in the interests of the Fund and its members that the contemplated increase in its resources be expedited, members are invited to comply as soon as possible with the procedure for notice and payments to the Fund under this First Resolution. Any payment made by a member before the effective date of increase in its quota will be kept in separate accounts of the Fund. If the Fund decides that such increase cannot become effective under this First Resolution, the payment will be returned to the member.

Second Resolution

1. The International Monetary Fund proposes that, subject to the provisions of this Second Resolution, the quotas of the following members shall be increased to the amounts shown against their names:

	Million U.S. dollars		*Million U.S. dollars*
1. Austria	175	9. Japan	725
2. Canada	740	10. Mexico	270
3. Finland	125	11. Norway	150
4. Germany, Federal Republic of	1,200	12. Philippines	110
5. Greece	100	13. South Africa	200
6. Iran	125	14. Spain	250
7. Ireland	80	15. Sweden	225
8. Israel	90	16. Venezuela	250

2. Paragraphs 2 through 7 of the First Resolution shall apply to this Second Resolution.

3. Members named in paragraph 1 of this Second Resolution shall be entitled to consent under either the First or the Second Resolution but not under both. Any such member shall declare under which Resolution it is consenting, and such choice shall be final.

Board of Governors Resolutions Nos. 20–6 and 20–7

Adopted March 31, 1965

Appendix II. EXECUTIVE DIRECTORS AND VOTING POWER on April 30, 1965

Director *Alternate*	Casting Votes of	Votes by Country	Total Votes[1]	Per Cent of Total
APPOINTED				
William B. Dale *John S. Hooker*	United States	41,500	41,500	22.48
J. M. Stevens *J. A. Kirbyshire*	United Kingdom	19,750	19,750	10.70
René Larre *Gérard M. Teyssier*	France	8,125	8,125	4.40
Ulrich Beelitz *Walter Habermeier*	Federal Republic of Germany	8,125	8,125	4.40
J. J. Anjaria *Arun K. Ghosh*	India	6,250	6,250	3.39
ELECTED				
Ahmed Zaki Saad (United Arab Republic) *Albert Mansour (United Arab Republic)*	Afghanistan Ethiopia Iran Iraq Jordan Kuwait Lebanon Pakistan Philippines Saudi Arabia Somalia Syrian Arab Republic United Arab Republic	475 400 950 800 362 750 317 1,750 1,000 800 362 500 1,450	9,916	5.37
Sergio Siglienti (Italy) *Costa P. Caranicas (Greece)*	Greece Italy Portugal Spain	850 5,250 850 1,750	8,700	4.71
J. M. Garland (Australia) *Roy Daniel (Australia)*	Australia New Zealand South Africa Viet-Nam	4,250 1,500 1,750 475	7,975	4.32
Gengo Suzuki (Japan) *Chalong Pungtrakul (Thailand)*	Burma Ceylon Japan Nepal Thailand	550 870 5,250 325 700	7,695	4.17
Pieter Lieftinck (Netherlands) *H. M. H. A. van der Valk (Netherlands)*	Cyprus Israel Netherlands Yugoslavia	362 750 4,375 1,450	6,937	3.76

Appendix II (*continued*). Executive Directors and Voting Power on April 30, 1965

Director *Alternate*	Casting Votes of	Votes by Country	Total Votes[1]	Per Cent of Total
Vacant	Canada	5,750		
S. J. Handfield-Jones (Canada)	Ireland	700		
	Jamaica	450	6,900	3.74
André van Campenhout (Belgium)	Austria	1,000		
Maurice Toussaint (Belgium)	Belgium	3,625		
	Korea	437		
	Luxembourg	400		
	Turkey	1,110	6,572	3.56
Maurício C. Bicalho (Brazil)	Brazil	3,050		
Antonio de Abreu Coutinho (Brazil)	Colombia	1,250		
	Dominican Republic	500		
	Haiti	362		
	Panama	362		
	Peru	625	6,149	3.33
Luis Escobar (Chile)	Argentina	3,050		
Enrique Domenech (Argentina)	Bolivia	475		
	Chile	1,250		
	Ecuador	450		
	Paraguay	362		
	Uruguay	550	6,137	3.32
Semyano Kiingi (Uganda)	Burundi	362		
Paul L. Faber (Guinea)	Congo, Democratic Rep. of	700		
	Guinea	400		
	Kenya	500		
	Liberia	362		
	Mali	380		
	Nigeria	750		
	Sierra Leone	362		
	Sudan	700		
	Tanzania	500		
	Trinidad and Tobago	450		
	Uganda	500	5,966	3.23
Enrique Tejera-Paris (Venezuela)	Costa Rica	450		
Jorge González del Valle (Guatemala)	El Salvador	450		
	Guatemala	400		
	Honduras	400		
	Mexico	2,050		
	Nicaragua	362		
	Venezuela	1,750	5,862	3.18

Appendix II (*concluded*). EXECUTIVE DIRECTORS AND VOTING POWER on April 30, 1965

Director *Alternate*	Casting Votes of	Votes by Country	Total Votes[1]	Per Cent of Total
Beue Tann (China)	China	5,750	5,750	3.12
I-Shuan Sun (China)				
Kurt Eklöf (Sweden)	Denmark	1,550		
Otto Schelin (Denmark)	Finland	820		
	Iceland	362		
	Norway	1,250		
	Sweden	1,750	5,732	3.11
Sumanang (Indonesia)	Algeria	850		
Amon Nikoi (Ghana)	Ghana	800		
	Indonesia	1,900		
	Laos	325		
	Libya	400		
	Morocco	775		
	Tunisia	475	5,525	2.99
Louis Kandé (Senegal)	Cameroon	400		
Antoine W. Yaméogo	Central African Republic	325		
(Upper Volta)	Chad	325		
	Congo (Brazzaville)	325		
	Dahomey	325		
	Gabon	325		
	Ivory Coast	400		
	Malagasy Republic	400		
	Mauritania	325		
	Niger	325		
	Rwanda	362		
	Senegal	500		
	Togo	362		
	Upper Volta	325	5,024	2.72
			184,590[2]	100.00

[1] Voting power varies on certain matters with use by members of the Fund's resources.
[2] This total does not include the votes of Malaysia, which was eligible to participate in the 1964 Regular Election of Executive Directors but abstained from voting.

Changes in the membership of the Executive Board between May 1, 1964 and April 30, 1965 were as follows:

Fernando Illanes (Chile) served as Temporary Alternate Executive Director to Guillermo Walter Klein (Argentina), May 1 to 11, 1964.

Alvin C. Lamb (Canada) served as Temporary Alternate Executive Director to A. F. W. Plumptre (Canada), May 1 and 22, July 10, and December 30, 1964, and January 22 to 25, March 10, and April 7, 1965.

Gérard M. Teyssier (France) served as Temporary Alternate Executive Director to Jean de Largentaye (France), May 1 to 13, 1964 and was appointed Alternate Executive Director to René Larre (France), effective June 1, 1964.

Jorge Mejía-Palacio (Colombia) served as Temporary Alternate Executive Director to Maurício C. Bicalho (Brazil), May 13, 1964.

Jacques Waïtzenegger (France) resigned as Alternate Executive Director to Jean de Largentaye (France), effective May 24, 1964.

John M. Garba (Nigeria) served as Temporary Alternate Executive Director to Louis Kandé (Senegal), June 3 and July 22 to August 5, 1964.

Joaquín Gutiérrez Cano (Spain) served as Temporary Alternate Executive Director to Sergio Siglienti (Italy), June 3 to 12, 1964 and January 6, 1965.

Julián Sáenz Hinojosa (Mexico) served as Temporary Alternate Executive Director to Práxedes Reina Hermosillo (Mexico), June 3 to 12 and September 26, 1964.

Jean de Largentaye (France) resigned as Executive Director for France, effective June 5, 1964.

René Larre (France) was appointed Executive Director for France, effective June 6, 1964.

Manuel Valladares (Mexico) served as Temporary Alternate Executive Director to Práxedes Reina Hermosillo (Mexico), June 17 and September 30 to October 2, 1964.

S. L. N. Simha (India) resigned as Alternate Executive Director to J. J. Anjaria (India), effective June 30, 1964.

Arun K. Ghosh (India) was appointed Alternate Executive Director to J. J. Anjaria (India), effective July 1, 1964.

Louis Plum (Belgium) served as Temporary Alternate Executive Director to André van Campenhout (Belgium), July 1 and 10, 1964 and April 21, 1965.

Carlos S. Brignone (Argentina) served as Temporary Alternate Executive Director to Guillermo Walter Klein (Argentina), July 10, 1964.

David C. Keys (United Kingdom) served as Temporary Alternate Executive Director to Sir Eric Roll (United Kingdom), July 29, August 3 to 5, October 14 to 16, and November 20, 1964 and to J. M. Stevens (United Kingdom), February 24, March 15, and April 21, 1965.

L. Denis Hudon (Canada) resigned as Alternate Executive Director to A. F. W. Plumptre (Canada), effective July 31, 1964.

S. J. Handfield-Jones (Canada) was appointed Alternate Executive Director to A. F. W. Plumptre (Canada), effective August 1, 1964 and was reappointed, effective November 1, 1964.

Sergio Bath (Brazil) served as Temporary Alternate Executive Director to Maurício C. Bicalho (Brazil), August 24 to 26, 1964.

Jean Malaplate (France) served as Temporary Alternate Executive Director to René Larre (France), August 24 and October 16, 1964, and March 31 and April 5, 1965.

Edgardo Sogno Rata del Vallino (Italy) served as Temporary Alternate Executive Director to Sergio Siglienti (Italy), August 26, 1964.

D. H. Boot (Netherlands) served as Temporary Alternate Executive Director to Pieter Lieftinck (Netherlands), September 26 to 30, 1964.

Guillermo Walter Klein (Argentina) completed his term of service as Executive Director for Argentina, Bolivia, Chile, Ecuador, Paraguay, and Uruguay, October 31, 1964.

Lennart Olofsson (Sweden) completed his term of service as Alternate Executive Director to Karl Skjaeveland (Norway), October 31, 1964.

Práxedes Reina Hermosillo (Mexico) completed his term of service as Executive Director for Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, and Venezuela, October 31, 1964.

Carlos Sansón (Nicaragua) completed his term of service as Alternate Executive Director to Práxedes Reina Hermosillo (Mexico), October 31, 1964.

Karl Skjaeveland (Norway) completed his term of service as Executive Director for Denmark, Finland, Iceland, Norway, and Sweden, October 31, 1964.

William Tennekoon (Ceylon) completed his term of service as Alternate Executive Director to Gengo Suzuki (Japan), October 31, 1964.

Mauríco C. Bicalho (Brazil) was re-elected Executive Director by Brazil, Colombia, the Dominican Republic, Haiti, Panama, and Peru, effective November 1, 1964.

Kurt Eklöf (Sweden) was elected Executive Director by Denmark, Finland, Iceland, Norway, and Sweden, effective November 1, 1964.

Otto Schelin (Denmark) was appointed Alternate Executive Director to Kurt Eklöf (Sweden), effective November 1, 1964.

Luis Escobar (Chile), formerly Alternate Executive Director to Guillermo Walter Klein (Argentina), was elected Executive Director by Argentina, Bolivia, Chile, Ecuador, Paraguay, and Uruguay, effective November 1, 1964.

Enrique Domenech (Argentina) was appointed Alternate Executive Director to Luis Escobar (Chile), effective November 1, 1964.

Alfonso Espinosa (Venezuela) was elected Executive Director by Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, and Venezuela, effective November 1, 1964 and resigned, effective February 11, 1965.

Jorge González del Valle (Guatemala) was appointed Alternate Executive Director to Alfonso Espinosa (Venezuela), effective November 1, 1964 and to Enrique Tejera-Paris (Venezuela), effective March 2, 1965.

J. M. Garland (Australia) was re-elected Executive Director by Australia, New Zealand, South Africa, and Viet-Nam, effective November 1, 1964.

Roy Daniel (Australia) was reappointed Alternate Executive Director to J. M. Garland (Australia), effective November 1, 1964.

Louis Kandé (Senegal) completed his term of service as Executive Director for Burundi, Cameroon, the Central African Republic, Chad, Congo (Brazzaville), the Democratic Republic of Congo, Dahomey, Gabon, Guinea, Ivory Coast, Liberia, the Malagasy Republic, Mali, Mauritania, Niger, Nigeria, Rwanda, Senegal, Sierra Leone, Tanzania, Togo, Trinidad and Tobago, Uganda, and Upper Volta, October 31, 1964 and was elected Executive Director by Cameroon, the Central African Republic, Chad, Congo (Brazzaville), Dahomey, Gabon, Ivory Coast, the Malagasy Republic, Mauritania, Niger, Rwanda, Senegal, Togo, and Upper Volta, effective November 1, 1964.

Antoine W. Yaméogo (Upper Volta) was appointed Alternate Executive Director to Louis Kandé (Senegal), effective November 1, 1964.

Semyano Kiingi (Uganda), formerly Alternate Executive Director to Louis Kandé (Senegal), was elected Executive Director by Burundi, the Democratic Republic of Congo, Guinea, Kenya, Liberia, Mali, Nigeria, Sierra Leone, the Sudan, Tanzania, Trinidad and Tobago, and Uganda, effective November 1, 1964.

Paul L. Faber (Guinea) was appointed Alternate Executive Director to Semyano Kiingi (Uganda), effective November 1, 1964.

Pieter Lieftinck (Netherlands) was re-elected Executive Director by Cyprus, Israel, the Netherlands, and Yugoslavia, effective November 1, 1964.

H. M. H. A. van der Valk (Netherlands) was reappointed Alternate Executive Director to Pieter Lieftinck (Netherlands), effective November 1, 1964.

A. F. W. Plumptre (Canada) completed his term of service as Executive Director for Canada and Ireland, October 31, 1964; he was elected Executive Director by Canada, Ireland, and Jamaica, effective November 1, 1964, and resigned, effective April 13, 1965.

Ahmed Zaki Saad (United Arab Republic) completed his term of service as Executive Director for Afghanistan, Ethiopia, Iran, Iraq, Jordan, Kuwait, Lebanon, Pakistan, the Philippines, Saudi Arabia, the Sudan, the Syrian Arab Republic, and the United Arab Republic, October 31, 1964 and was elected Executive Director by Afghanistan, Ethiopia, Iran, Iraq, Jordan, Kuwait, Lebanon, Pakistan, the Philippines, Saudi Arabia, Somalia, the Syrian Arab Republic, and the United Arab Republic, effective November 1, 1964.

Sergio Siglienti (Italy) was re-elected Executive Director by Greece, Italy, Portugal, and Spain, effective November 1, 1964.

Costa P. Caranicas (Greece) was reappointed Alternate Executive Director to Sergio Siglienti (Italy), effective November 1, 1964.

Sumanang (Indonesia) completed his term of service as Executive Director for Ghana, Indonesia, Laos, Libya, Malaysia, Morocco, and Tunisia, October 31, 1964 and was elected Executive Director by Algeria, Ghana, Indonesia, Laos, Libya, Morocco, and Tunisia, effective November 1, 1964.

Gengo Suzuki (Japan) was re-elected Executive Director by Burma, Ceylon, Japan, Nepal, and Thailand, effective November 1, 1964.

Chalong Pungtrakul (Thailand) was appointed Alternate Executive Director to Gengo Suzuki (Japan), effective November 1, 1964.

Beue Tann (China) was re-elected Executive Director for China, effective November 1, 1964.

André van Campenhout (Belgium) was re-elected Executive Director by Austria, Belgium, Korea, Luxembourg, and Turkey, effective November 1, 1964.

Carlos Pérez de la Cova (Venezuela) served as Temporary Alternate Executive Director to Alfonso Espinosa (Venezuela), November 30, 1964.

Sir Eric Roll (United Kingdom) resigned as Executive Director for the United Kingdom, effective January 14, 1965.

J. M. Stevens (United Kingdom) was appointed Executive Director by the United Kingdom, effective January 15, 1965.

J. A. Kirbyshire (United Kingdom), formerly Alternate Executive Director to Sir Eric Roll (United Kingdom), was appointed Alternate Executive Director to J. M. Stevens (United Kingdom), effective January 15, 1965.

Rufino Gil (Costa Rica) served as Temporary Alternate Executive Director to Jorge González del Valle (Guatemala), February 24 to 26, 1965 and to Enrique Tejera-Paris (Venezuela), March 15, 1965.

W. Y. Hui (China) served as Temporary Alternate Executive Director to Beue Tann (China), February 26 to April 21, 1965.

Enrique Tejera-Paris (Venezuela) was elected Executive Director by Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, and Venezuela, effective March 2, 1965.

S. J. Handfield-Jones (Canada) was elected Executive Director by Canada, Ireland, and Jamaica, effective May 1, 1965.

Appendix IV. Administrative Budget

Letter of Transmittal

July 2, 1965

My dear Mr. Chairman:

The administrative budget of the Fund approved by the Executive Board for the Fiscal Year ending April 30, 1966 is presented herewith, in accordance with Section 20 of the By-Laws. The presentation also shows actual expenditures for the past two fiscal years.

I should like to reiterate that it is of course impossible to predict whether the amounts budgeted will, in fact, meet the requirements of the Fund's program. The amounts shown are estimates of requirements on the basis of the expected level of activities. Should contingencies arise or present plans change materially, the management would recommend appropriate amendments to the Executive Board.

Yours sincerely,
/s/
P.-P. Schweitzer
Chairman of the Executive Board

Chairman of the Board of Governors
International Monetary Fund

Administrative Budget as Approved by the Executive Board for the Fiscal Year Ending April 30, 1966, Compared with Actual Expenditures for the Fiscal Years 1963-64 and 1964-65

Category of Expenditure	Budget F.Y. 1965-66	F.Y. 1964-65 Budget	F.Y. 1964-65 Actual Expenditures	Actual Expenditures F.Y. 1963-64
I. Board of Governors	$ 420,000	$ 874,000	$ 864,824	$ 367,657
II. Office of Executive Directors				
Salaries	1,055,000	1,018,500	1,002,451	956,715
Other compensations and benefits	197,000	208,500	189,568	195,669
Travel	203,000	269,000	227,422	180,363
Total	$ 1,455,000	$ 1,496,000	$ 1,419,441	$ 1,332,747
III. Staff				
Salaries	$ 6,755,000	$ 5,744,000	$ 5,648,798	$ 4,770,520
Other compensations and benefits	2,163,000	1,996,000	1,901,081	1,768,625
Travel	1,375,000	1,375,000	1,279,519	1,199,041
Total	$10,293,000	$ 9,115,000	$ 8,829,398	$ 7,738,186
IV. Special Services to Member Countries	$ 925,000	$ 682,000	$ 352,445	—
V. Other Administrative Expenses				
Communications	$ 347,000	$ 314,000	$ 304,250	$ 297,165
Office occupancy expenses	685,000	548,000	531,789	473,713
Books and printing	320,000	259,000	247,930	177,954
Supplies and equipment	408,000	241,000	223,862	202,796
Miscellaneous	307,000	266,000	237,535	285,905
Total	$ 2,067,000	$ 1,628,000	$ 1,545,366	$ 1,437,533
Total	$15,160,000	$13,795,000	$13,011,474	$10,876,123

Appendix V. Comparative Statement of Income and Expenditure

(Values expressed in U.S. dollars on the basis of established parities)

	Year Ended Apr. 30, 1963	Year Ended Apr. 30, 1964	Year Ended Apr. 30, 1965
INCOME [1]			
Service charges			
Received in gold	$ 2,774,861	$ 2,504,482	$ 1,274,187
Received in members' currencies	125,000	625,000	8,213,000
Total	$ 2,899,861	$ 3,129,482	$ 9,487,187
Charges on Fund's holdings of members' currencies and securities in excess of quotas			
Received in gold	$19,940,415	$25,430,807	$26,167,091
Received in members' currencies	4,533,900	6,068,948	9,738,818
Total	$24,474,315	$31,499,755	$35,905,909
Other operational income	$ 3,669,065	$ 1,721,254	$ 2,353,709
Miscellaneous income	1,176	1,581	2,257
TOTAL INCOME	$31,044,417	$36,352,072	$47,749,062
EXPENDITURE			
Administrative	$ 9,401,011	$10,876,123	$13,011,474
Operational	1,655	115 Cr.	4,557,523
Fixed property	167,038	2,182,015	4,635,295
Contribution to The Per Jacobsson Foundation	—	62,500	—
TOTAL EXPENDITURE	$ 9,569,704	$13,120,523	$22,204,292

[1] Excludes income from investments transferred to Special Reserve for the fiscal years ended April 30, as follows:

1963	$25,094,232
1964	27,485,414
1965	30,750,435

Appendix VI

FINANCIAL STATEMENTS

Page

Letter of Transmittal 144

FINANCIAL STATEMENTS OF INTERNATIONAL MONETARY FUND

Memorandum by the Audit Committee 145
Exhibit A—Balance Sheet as at April 30, 1965 146
Exhibit B—Statement of Income and Expenditure for the Year Ended April 30, 1965 148
Exhibit C—Statement of Reserves for the Year Ended April 30, 1965 149

FINANCIAL STATEMENTS OF STAFF RETIREMENT FUND

Memorandum by the Audit Committee 150
Exhibit I—Balance Sheet as at April 30, 1965 152

Appendix VI. FINANCIAL STATEMENTS OF INTERNATIONAL MONETARY FUND AND STAFF RETIREMENT FUND

Letter of Transmittal

July 2, 1965

My dear Mr. Chairman:

In accordance with Section 20(b) of the By-Laws of the Fund, I have the honor to submit for the consideration of the Board of Governors the audited financial statements of the International Monetary Fund, and the Staff Retirement Fund, for the year ended April 30, 1965, together with two memoranda from the Audit Committee, which include the audit certificates.

In conformity with the By-Laws, the external audit of the Fund has been performed by an Audit Committee consisting of auditors nominated by three member countries. At the Fund's request, El Salvador, Thailand, and the United Kingdom nominated auditors to serve on this Committee. They respectively nominated Mr. Juan Samuel Quinteros, Superintendent, Superintendency of Banks and Other Financial Institutions, Central Bank of El Salvador; Mr. Panas Simasathien, Chief of Accounting and Fiscal Systems Division, Comptroller General's Department, Ministry of Finance, Thailand; and Mr. Ronald William Tizard, Deputy Director of Audit, Exchequer and Audit Department, United Kingdom. The Auditors thus nominated were confirmed by the Executive Directors.

It will be noted that, in the period under review, ordinary income amounted to $47,749,062 and expenditure amounted to $22,204,292, resulting in a net income of $25,544,770, which has been transferred provisionally to General Reserve pending Board of Governors' action. In addition, income of $30,750,435 from the Fund's investment program has been transferred to the Special Reserve.

The detailed report of the Audit Committee is being submitted separately to the Board of Governors.

Yours sincerely,
/s/
P.-P. SCHWEITZER
Chairman of the Executive Board

Chairman of the Board of Governors
International Monetary Fund

Memorandum by the Audit Committee

June 22, 1965

To the Managing Director
and the Executive Directors
International Monetary Fund

The report of the Audit Committee, dated June 22, 1965, submitted through you to the Board of Governors, on the audit of the financial records and transactions of the Fund for the fiscal year ended April 30, 1965, includes the following paragraphs relating to the scope of the audit conducted, and the audit certificate given:

Scope of the Audit

The Audit Committee, in the conduct of its audit, took cognizance of the requirements of Section 20(b) of the By-Laws that the audit be comprehensive with respect to the examination of the financial records of the Fund; that it extend, insofar as practicable, to the ascertainment that financial transactions consummated during the period under review were supported by the necessary authority; and that it determine that there was adequate and faithful accounting for the assets of the Fund. In determining the authority for financial transactions, reference was made to the Articles of Agreement, the By-Laws and Rules and Regulations of the Fund, the minutes of the Executive Board and the General Administrative Orders of the Fund. The Committee applied such tests to the accounting and other financial records as it considered necessary to provide a thorough review of the adequacy of the system of accounting and internal control operated by the Fund. In determining its program of test examination, due regard was paid to the work performed by the Internal Auditor, as reported by him to the Committee, and to the standard of his work performance as surveyed by the Committee.

Audit Certificate

We have made an independent examination of the Balance Sheet of the International Monetary Fund as at April 30, 1965, of the Statements of Income and Expenditure and of Reserves for the fiscal year then ended and of the schedules related to such financial statements. We have obtained from the officers and staff of the Fund all such information and representations as we have required in the conduct of our audit.

As the result of our examination, we report that, in our opinion, such Balance Sheet and related Statement of Income and Expenditure, together with the notes appearing thereon, present fairly the financial position of the International Monetary Fund as at April 30, 1965, and the results of its operations for the fiscal year then ended, and have been prepared in conformity with generally accepted accounting principles applied on a basis consistent with that of previous fiscal years.

Audit Committee:

/s/ Juan Samuel Quinteros, Chairman (El Salvador)

/s/ Panas Simasathien (Thailand)

/s/ R. W. Tizard (United Kingdom)

Appendix VI (*continued*)

Exhibit A

BALANCE

as at April

Values expressed in U.S. dollars on the

ASSETS

GOLD ACCOUNT			
Gold with depositories (See Note 2)		$2,217,252,733	
(63,350,078.086 fine ounces at $35 per ounce)			
Investments (See Note 3)			
$823,532,000 U.S. Government securities maturing within 12 months, at cost	$799,835,379		
Funds awaiting investment	156,132	799,991,511	$ 3,017,244,244
CURRENCIES AND SECURITIES			
With depositories			
Currencies		$2,786,151,051	
Securities		9,953,189,074	12,739,340,125
(nonnegotiable, noninterest-bearing demand obligations, payable at face value by members in their currencies)			
SUBSCRIPTIONS TO CAPITAL—RECEIVABLE			
Balances not due			903,876,735
WITHDRAWING MEMBER'S CURRENCY			9,999,861
(redeemable by Cuba in gold, or convertible currencies acceptable to the Fund, in five equal annual installments commencing July 1, 1964)			
OTHER ASSETS (See Note 4)			21,801,271
(receivables, accruals, prepayments, and sundry cash)			
TOTAL ASSETS			$16,692,262,236

NOTES:

1. With the exception of the following currencies which, for bookkeeping purposes, are computed at the following provisional rates per U.S. dollar:

Argentine peso	83.0000	Colombian peso	9.00000	Paraguayan guaraní	122.000
Bolivian peso	11.8750	Indonesian rupiah	315.000	Peruvian sol	26.8150
Brazilian cruzeiro	470.000	Korean won	255.000	Vietnamese piastre	35.0000
Chilean escudo	2.70000	Mali franc	246.853	Yuglosav dinar	750.000

2. Excludes 10,597.227 fine ounces earmarked for members.

3. Made with the proceeds of the sale of 22,856,900.312 fine ounces of gold. Upon termination of the investment, the same quantity of gold can be reacquired.

4. The assets and liabilities of the Staff Retirement Fund are not included in this Balance Sheet.

5. A stand-by charge has, under certain circumstances, to be credited against the service charge for a drawing under the stand-by arrangement; the maximum amount on April 30, 1965 is $868,959. A portion of the stand-by charge is refundable to a member if the arrangement is canceled; the maximum amount on April 30, 1965 is $661,264.

Exhibit A

SHEET

30, 1965

basis of established parities (See Note 1)

CAPITAL, RESERVES, AND LIABILITIES

CAPITAL		
Authorized subscriptions of members		$15,993,083,333
RESERVES (Exhibit C)		
Special reserve	$148,274,447	
General reserve	141,811,468	290,085,915
INDEBTEDNESS TO PARTICIPANTS UNDER GENERAL ARRANGEMENTS TO BORROW		405,000,000
PROVISION FOR POTENTIAL REFUNDS OF STAND-BY CHARGES (See Note 5)		868,959
OTHER LIABILITIES (See Note 4) (*accruals, payables, and deferred credits*)		3,224,029
TOTAL CAPITAL, RESERVES, AND LIABILITIES		$16,692,262,236

/s/ Y. C. KOO
Treasurer

/s/ P.-P. SCHWEITZER
Managing Director

/s/ C. M. POWELL
Comptroller and Assistant Treasurer

Exhibit B

Statement of Income and Expenditure
for the year ended April 30, 1965

INCOME			
Operational charges		$11,840,896	
Charges on balances in excess of quotas		35,905,909	
Other income		2,257	
TOTAL INCOME (See Note 1)			$47,749,062
EXPENDITURE			
Administrative expenditure			
Board of Governors		$ 864,824	
Office of Executive Directors			
Salaries	$1,002,451		
Other compensations and benefits	189,568		
Travel	227,422	1,419,441	
Staff			
Salaries	$5,648,798		
Other compensations and benefits	1,901,081		
Travel	1,279,519	8,829,398	
Special services to member countries			
IMF Institute's Program	$167,315		
Technical assistance to the Democratic Republic of Congo	88,054		
Panel of Central Banking Experts	97,076	352,445	
Other administrative expenses			
Communications	$304,250		
Office occupancy	531,789		
Books and printing (See Note 2)	247,930		
Supplies and equipment	223,862		
Miscellaneous (See Note 3)	237,535	1,545,366	
Total administrative expenditure		$13,011,474	
Operational expenditure			
Transfer charges on amounts borrowed under General Arrangements to Borrow	$2,025,000		
Interest on indebtedness under General Arrangements to Borrow	2,531,250		
Gold handling costs	1,630		
Exchange adjustments	357 cr.		
Total operational expenditure		4,557,523	
Fixed property expenditure		4,635,295	
TOTAL EXPENDITURE			22,204,292
NET INCOME (Transferred provisionally to General Reserve pending Board of Governors' action) (Exhibit C)			$25,544,770

NOTES:
1. Excludes income from investments amounting to $30,750,435, transferred to Special Reserve (Exhibit C).
2. After deduction of $64,182 for sales of Fund's publications.
3. After deduction of $115,069 for food service sales.

Exhibit C

Statement of Reserves

for the year ended April 30, 1965

Special Reserve (See Note)		
Balance, April 30, 1964	$117,524,012	
Add		
Income from investments in U.S. Government securities for year	30,750,435	
Balance, April 30, 1965		$148,274,447
General Reserve		
Balance, April 30, 1964	$116,518,698	
Add		
Net income for year (Exhibit B), transferred provisionally pending Board of Governors' action	25,544,770	
	$142,063,468	
Deduct		
Transfer to Staff Retirement Plan for past service cost relating to previous fiscal years resulting from February 5, 1965 amendment to the Plan	252,000	
Balance, April 30, 1965		141,811,468
Total Reserves (per Balance Sheet)		$290,085,915

Note:
Represents income from investments in U.S. Government securities from November 1, 1957.

Staff Retirement Fund

Memorandum by the Audit Committee

June 22, 1965

To the Managing Director
and the Executive Directors
International Monetary Fund

The report of the Audit Committee, dated June 22, 1965, submitted through you to the Board of Governors, on the audit of the financial records and transactions of the International Monetary Fund for the fiscal year ended April 30, 1965, includes the following paragraphs relating to the scope of the audit conducted, the audit certificate given and the investments held with respect to the Staff Retirement Fund:

Scope of the Audit

The Audit Committee has examined the separate accounts and financial statements relating to the Staff Retirement Fund for the fiscal year ended April 30, 1965. In the course of the examination, the Committee referred to the Articles of the Staff Retirement Plan and to the decisions of the Pension, Administration and Investment Committees created under the Plan. The Audit Committee made what it considered an adequate test check of the various classes of transactions, taking into account the audit coverage made by the Internal Auditor, as reported by him to the Committee. The report of the Internal Auditor, among other audit activities conducted by his staff, showed that a detailed examination had been made of the Participants' Accounts.

Audit Certificate

As the result of our examination, we report that in our opinion the accompanying Balance Sheet, Statement of Source and Application of Funds, and the related Schedules of Participants' Account, Accumulation Account, Retirement Reserve Account, and Reserve Against Investments present fairly the financial position of the Staff Retirement Fund as at April 30, 1965 and the results of its operations for the fiscal year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of previous fiscal years.

Investments

Two amendments of the General Rules on Investment were made by the Pension Committee during the fiscal year 1965. On March 22, 1965 the Pension Committee adopted the Investment Committee's recommendation that the ceiling on corporate stocks held in the Staff Retirement Plan portfolio be raised from 35 per cent to 40 per cent of the original investment. And on April 12, 1965 the Pension Committee approved the bonds of the Inter-American Development Bank as securities eligible for investment.

A confirmation was received by the Audit Committee directly from the depository concerning the investments it held, as at April 30, 1965, as custodian for the Staff

Retirement Fund of the International Monetary Fund. The Audit Committee confirmed that the holdings of the various classes of investments were within the limiting percentages prescribed by the Pension Committee, as follows:

	Authorized Percentage	*Actual Percentage*	*Original Investment*
Bonds			
U.S. Government	Minimum 30	38.84	$ 5,857,817
International Bank for Reconstruction and Development and Inter-American Development Bank	Maximum 20	12.60	1,900,805
Corporate (other than convertible)	Maximum 25	14.81	2,234,607
Corporate (convertible)	Maximum 5	—	—
Total Bonds		66.25	$ 9,993,229
Corporate stocks	Maximum 40	33.75	5,089,979
Total Portfolio		100.00	$15,083,208

AUDIT COMMITTEE:

/s/ Juan Samuel Quinteros, Chairman (El Salvador)

/s/ Panas Simasathien (Thailand)

/s/ R. W. Tizard (United Kingdom)

Appendix VI (*concluded*)

Exhibit I

STAFF RETIREMENT FUND

BALANCE SHEET
as at April 30, 1965

ASSETS

CASH AT BANKS			$ 77,203
INVESTMENTS			
Bonds, at amortized value			
United States Government (*market value, $5,620,000*)	$5,632,034		
International Bank for Reconstruction and Development (*market value, $1,841,780*)	1,838,750		
Corporate (*market value, $2,063,940*)	2,208,839	$9,679,623	
Corporate stocks (common), at cost (*market value, $9,291,490*)		5,813,409	15,493,032
ACCRUED INTEREST ON BONDS			102,157
ACCRUED CONTRIBUTIONS FROM PARTICIPANTS AND EMPLOYER			10,621
TOTAL ASSETS			$15,683,013

LIABILITIES AND RESERVES

ACCOUNTS PAYABLE	$ 4,480
PARTICIPANTS' ACCOUNT	3,372,179
ACCUMULATION ACCOUNT	10,395,030
RETIREMENT RESERVE ACCOUNT	1,501,498
RESERVE AGAINST INVESTMENTS	409,826
TOTAL LIABILITIES AND RESERVES	$15,683,013

/s/ Y. C. KOO
Treasurer

/s/ C. M. POWELL
Comptroller and Assistant Treasurer

/s/ P.-P. SCHWEITZER
Managing Director

INDEX

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INDEX

Numbers refer to pages. An asterisk (*) denotes a table, a dagger (†) denotes a chart.

AFGHANISTAN—Fund quota, proposed increase in, 129*; transaction with Fund, 108*

AFRICAN COUNTRIES—debt servicing problems, 24*, 25*, 26†; personal taxes, 23; *see also* individual countries

ALGERIA—Fund quota, proposed increase in, 129*

ARGENTINA—balance of payments and reserves, 67*, 74*, 75, 76*; debt servicing problems, 26†, 29, 75; devaluation of currency, 75; exchange controls, 75; Fund quota, proposed increase in, 129*; gold policy, 102; inflation, 78; monetary policies, 78; public enterprises, 23; transaction with Fund, 112*

ASIA, EAST—debt servicing problems, 24*, 25*, 26†

AUSTRALIA—balance of payments and reserves, 59, 67*, 73, 74*, 76*, 91; capital movements, 50, 91; currency used in Fund transactions, 35, 113; economic expansion, 91; exports and export markets, 53; Fund Article VIII, acceptance of, 31, 107; Fund quota, proposed increase in, 129*; gold production, 96*, 97, 102; gold subsidy program, 103; monetary policy, 91; prices, 91; unemployment, 91

AUSTRIA—balance of payments and reserves, 63*, 67*; currency purchased by Fund with gold, 108*; currency used in Fund transactions, 35, 113*; exports and export markets, 57, 58*; Fund Article VIII, acceptance of, 107*; Fund holding of currency, 112; Fund quota, proposed increases in, 32*, 129*; gold purchases from U.S., 99*

BALANCES OF PAYMENTS—4-6, 63-68; industrial countries, 79-90; primary producing countries, 71-78, 91-95

BANK FOR INTERNATIONAL SETTLEMENTS—Fund relations with, 117; gold holdings, 69, 97, 99*; support for sterling, 4

BANKS—*see* Interest Rates; Monetary Policy

BELGIUM—currency purchased by Fund with gold, 108*; currency used in Fund transactions, 113; fiscal policy, 47; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; General Arrangements to Borrow, 108*; gold prices, 101*; gold purchases from U.S., 99*; industrial production, 42†; interest rates, 45, 46; monetary policy, 46; *see also* Belgium-Luxembourg

BELGIUM-LUXEMBOURG — balance of payments and reserves, 62*, 65, 67*; exports and export markets, 57, 58*; prices, 57

BOLIVIA—balance of payments and reserves, 76*; debt servicing problems, 26†; Fund quota, proposed increase in, 129*; gold production, 97; transactions with Fund, 109*, 111, 112*

BRAZIL—balance of payments and reserves, 67*, 74*, 76*, 91-92; budget deficit, 78; capital movements, 92; debt servicing problems, 23, 26†, 29, 30, 92; Fund quota, proposed increase in, 129*; gold sales to U.S., 99*; inflation, 78, 91, 110; monetary policies, 78, 92; public enterprises, 23, 92; transactions with Fund, 7, 108*, 109*, 110, 112*

BURMA—balance of payments and reserves, 76*; Fund quota, proposed increase in, 129*

BURUNDI—Fund quota, proposed increase in, 129*; initial par value agreed, 107*, 110; stabilization measures, 78, 110; transactions with Fund, 35, 108*, 109*, 110

CAMEROON—Fund quota, proposed increase in, 129*

CANADA—balance of payments and reserves, 59, 67*, 74*, 76*, 82-83; capital movements, 50, 61, 82-83; currency purchased by Fund with gold, 108*; currency used in Fund transactions, 35, 113*, 114*; exports and export markets, 53, 59, 71; Fund Article VIII, acceptance of, 107*; Fund holding of dollars, 112; Fund quota, proposed increases in, 32*, 129*; General Arrangements to Borrow, 108*; gold production, 96*, 97; gold subsidy program, 102; gross national product, increases in, 42*; industrial production, 43*; interest rates, 45-46, 49; prices, 43-44, 53*; transactions with Fund, 20, 112, 113*; unemployment, 3; wages, 43

CAPITAL MARKETS—12-13, 50-52; in developing countries, 21

CAPITAL MOVEMENTS—6, 12-13, 60-63; *see also* balance of payments of individual countries

CENTRAL AFRICAN REPUBLIC—Fund quota, proposed increase in, 129*

CEYLON—balance of payments and reserves, 71, 74*, 76*; Fund quota, increase in, 107, 108*; Fund quota, proposed increase in, 129*; public enterprises, 23; transactions with Fund, 108*, 112*

CHAD—Fund quota, proposed increase in, 129*

CHILE—balance of payments and reserves, 71, 74*, 76*; debt servicing problems, 26†, 29; Fund quota, proposed increase in, 129*; inflation, 78; monetary policies, 78; transactions with Fund, 108*, 109*, 111, 112*

CHINA, REPUBLIC OF—balance of payments and reserves, 75, 76*; Fund quota, proposed increase in, 129*

COCOA—71, 72†, 92-93

COFFEE—71, 72†, 74*

COLOMBIA—balance of payments and reserves, 71, 74*, 76*; debt servicing problems, 26†; Fund quota, proposed increase in, 129*; gold production, 96; transactions with Fund, 108*, 109*, 112*

CONGO (BRAZZAVILLE)—Fund quota, proposed increase in, 129*

CONGO, DEMOCRATIC REPUBLIC OF—Fund quota, proposed increase in, 129*; Fund technical assistance, 36; gold production, 96

COPPER—72†

COSTA RICA—balance of payments and reserves, 76*; Fund Article VIII, acceptance of, 31, 107, 110; Fund quota, increase in, 107, 108*; Fund quota, proposed increase in, 129*; transactions with Fund, 108*, 109*, 110, 112*

COTTON—71, 72†

CYPRUS—balance of payments and reserves, 76*; Fund quota, proposed increase in, 129*; transaction with Fund, 35, 108*

DAHOMEY—Fund quota, proposed increase in, 129*

DEBT MANAGEMENT—industrial countries, 45-46

DEBT SERVICING PROBLEMS—in primary producing countries, 7, 23-30; renegotiation, 26-30; repayment schedules, 24-25; role of Fund, 29-30

DENMARK—balance of payments and reserves, 63*, 67*; capital movements, 51*; currency purchased by Fund with gold, 108*; exports and export markets, 58*; Fund quota, proposed increase in, 129*; interest rates, 45, 46; monetary policy, 46

DEVELOPING COUNTRIES—*see* Primary Producing Countries

DOMINICAN REPUBLIC — balance of payments and reserves, 76*; economic policies, 110; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; transactions with Fund, 108*, 109*, 110

DRAWINGS—*see* Fund Transactions: currency purchases

ECUADOR—balance of payments and reserves, 76*; Fund quota, proposed increase in, 129*; tax reform, 23; transactions with Fund, 108*, 109*, 111, 112*

EL SALVADOR—balance of payments and reserves, 76*; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; transaction with Fund, 109*

ETHIOPIA—balance of payments and reserves, 76*; Fund quota, proposed increase in, 129*

EURO-DOLLAR MARKET—12, 50, 60

EUROPE—balance of payments and reserves, 12, 67*; capital markets, 50;

capital movements, 12, 51*, 61; debt servicing problems in southern Europe, 24*, 25*, 26†; economic expansion, 4; exports and export markets, 56*, 59; prices, 6, 44; unemployment, 11; wages, 44; *see also* individual countries
EUROPEAN ECONOMIC COMMUNITY—balance of payments and reserves, 4, 59†, 60†, 62*, 63, 64†, 65, 66, 67-68; capital movements, 61; exports and export markets, 54, 55, 56, 57*, 58, 59; industrial production, 41†, 42; prices, 44, 53*; wages, 43†; *see also* individual member countries
EUROPEAN FREE TRADE ASSOCIATION—balance of payments and reserves, 59†; prices, 53*; *see also* individual member countries
EUROPEAN FUND—gold holdings, 69, 97, 99*
EXCHANGE RATES—11, 36, 47
EXCHANGE RESERVES—creation of additional, 16, acceptability, 16-17, criteria, 16, distribution, 17-18, institution for, 18, and transfer of real resources, 18, transferability, 16-17, through the Fund, 18-19; reserve center currencies, 9, 10, 13-14; *see also* Reserves, Gold and Foreign Exchange
EXPORT PRICES—*see* Prices
EXPORTS—performance of manufacturing countries, 53-60; performance of primary producing countries, 71
EXPORTS AND EXPORT MARKETS—54-58

FINANCIAL POLICIES—industrial countries, 45-46
FINLAND—balance of payments and reserves, 67*, 71, 73, 74*, 76*; capital movements, 51*; Fund quota, proposed increases in, 32*, 129*
FISCAL SYSTEMS—improvements, 22-23, budgetary control, 22, public enterprises, 23, tax administration, 23, tax reform, 22-23; in primary producing countries, 21-23
FOREIGN EXCHANGE MARKETS—50
FOREIGN EXCHANGE RESERVES—*see* Exchange Reserves; Reserves, Gold and Foreign Exchange
FOREIGN TRADE—*see* balance of payments of individual countries *and* World Trade
FRANCE—balance of payments and reserves, 62*, 64†, 67*, 85-88; capital market, 51*, 52; capital movements, 85-88; currency purchased by Fund with gold, 108*; currency used in Fund transactions, 35, 113, 114*; currency used in international transactions, 9; economic expansion, 42; economic policies, 3, 42; exchange rate, 47†; exports and export markets, 58*; fiscal situation and policy, 47; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; General Arrangements to Borrow, 108*; gold and foreign exchange reserves, 88, 100; gold prices, 101*, 102; gold purchases from U.S., 88, 99*; industrial production, 3, 42, 43*; inflation, 42, 85, 86; interest rates, 45†, 49; monetary policy, 46; prices, 3, 42, 57; transactions with Fund, 20; wages, 43†
FUND ADMINISTRATIVE BUDGET AND EXPENDITURE—119, 138
FUND ARTICLES OF AGREEMENT—9, 10, 12, 15; Article I, 20; Article III, Section 4, 33; Article V, Section 3, 33, 35; Article V, Section 4, waivers under, 111; Article V, Section 7, 35, 111-12, 113, 114; Article V, Section 8, 116; Article VII, Section 2, 34; Article VIII, 12, 31, 107*, 110, 117; Article XIV, 116-17
FUND AUDIT COMMITTEE—members, 119
FUND BALANCE SHEET—146-47
FUND CHARGES—116
FUND CONSULTATIONS WITH MEMBERS—116-17
FUND COOPERATION WITH OTHER INTERNATIONAL ORGANIZATIONS—7, 8, 36, 117-18
FUND DEPARTMENTS—Central Banking Service, 8, 36; Exchange and Trade Relations Department, 118; Fiscal Affairs Department, 8, 22, 36; IMF Institute, 37
FUND EXECUTIVE BOARD—election of additional Director, 31; membership and voting power, 133-39
FUND EXECUTIVE BOARD DECISIONS—Article VIII and Article XIV, 116-17; compensatory financing of export fluctuations, 7, 32, 33, 107, 108; currencies to be used in transactions, 34, 35; gold subscriptions, 8, 33-34; procedure for drawings in the gold tranche, 10, 35, 119; reporting of monetary reserves data, 113; use of Fund's resources and repurchases, 10, 33, 112
FUND FINANCIAL STATEMENTS—119, 140-52
FUND GOLD HOLDINGS—investment of, 119, 146
FUND GOLD TRANSACTIONS—5, 34, 35, 48, 69, 99*, 113*
FUND MEMBERS—acceptance of obligations of Article VIII, 31, 107*; applications to become, 31; convertibility of currencies, 12; gold tranche positions, 10, 18, 33, 68*; number of, 31; par values, 107; reporting of monetary reserves data, 113-14; repurchase obligations, 35, 113-14
FUND PUBLICATIONS—118-19
FUND QUOTAS—increases in, 8, 14-15, 31-33, 107-108, 124-32, and alleviations of gold payments, 8, 33-34, and installment facility, 33, and special drawing facility, 33; new members, 31
FUND RESOURCES—compensatory financing facility, 7, 32, 33, 107, 108; conditional liquidity, 10, 14-15, 18; creation of international liquidity, 15, 17, 18-19; debt renegotiations, 29; use of, *see* Fund Transactions
FUND STAFF—118
FUND TECHNICAL ASSISTANCE TO MEMBERS—*see* Fund Departments
FUND TRAINING PROGRAM—37
FUND TRANSACTIONS—amounts outstanding, 115†; as reserve transfers, 17; before establishment of par value, 36; currencies used, 35, 112-13; currency purchases by members, 7, 20, 34-36, 108*, 109, 112*, 113*; currency purchases by Fund, 5, 34-35, 97*, 108*; currency repurchases by members, 111-16; gold tranche drawings, 10, 35; stand-by arrangements, 7, 34-36, 109-11, 115†; stand-by arrangements and debt renegotiation, 29-30; summary, 114-16; *see also* General Arrangements to Borrow

GABON—Fund quota, proposed increase in, 129*
GENERAL AGREEMENT ON TARIFFS AND TRADE—9, 12; Fund cooperation with, 117, 118
GENERAL ARRANGEMENTS TO BORROW—borrowings under, 4-5, 8, 34, 35, 48, 108*, 109; charges paid by Fund, 116; constitutes reserves, 10, 17, 19, 68*, 69
GERMANY, FEDERAL REPUBLIC OF—balance of payments and reserves, 59, 60†, 62*, 64†, 65, 67*, 68, 85, 86*; capital market, 50, 51*, 52; capital movements, 85, 86*; currency purchased by Fund with gold, 108*; currency used in Fund transactions, 35, 113*, 114*; economic expansion, 3, 4, 42, 85; exchange rate, 47†; exports and export markets, 54, 57, 58*; fiscal policy, 51-52, 85; Fund Article VIII, acceptance of, 107*; Fund holdings of deutsche mark, 112; Fund quota, proposed increases in, 32*, 129*; General Arrangements to Borrow, 108*; gold purchases from U.S., 99*; gross national product, increases in, 42*; industrial production, 42†, 43*; interest rates, 45, 49; monetary policy, 46; prices, 3, 57; productivity, 43; wages, 43
GHANA—balance of payments and reserves, 76*, 92-93; budget, 92-93; capital movements, 93; cocoa production, 92-93; Fund quota, increase in, 107, 108*; Fund quota, proposed increase in, 129*; gold and foreign exchange reserves, 93; gold production, 96*, 97; prices, 93; wages, 93
GOLD—absorption by private holders, industry, and arts, 8, 98†, 99; coins, prices of, 101*; Fund's holdings, 97, 99, 146; markets and prices, 99-102; national policies affecting, 96, 100-101, 102-103; pool, 9-10, 99, 100, 101, 102; price as basis for monetary system, 10, 15, 99; production, 69, 96-97, 98†; reserves,

68*, 69, 98†, 99*; Soviet production, reserves, and sales, 69, 98†, 99*; subsidy programs, 102-103; transactions service of Fund, 102; used in Fund transactions, 5, 34-35, 99*, 108*, 113*, 114*
GOLD EXCHANGE STANDARD—14, 15
GOLD STANDARD—11
GREECE—balance of payments and reserves, 76*; Fund quota, proposed increases in, 32*, 129*; monetary policies, 78
GUATEMALA—balance of payments and reserves, 76*; Fund Article VIII, acceptance of, 107*; Fund quota, increase in, 107, 108; Fund quota, proposed increase in, 129*
GUINEA—Fund quota, proposed increase in, 129*

HAITI—balance of payments and reserves, 76*; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; transactions with Fund, 108*, 109*, 111
HONDURAS—balance of payments and reserves, 76*; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; transactions with Fund, 108*, 109*, 111, 112*
HONG KONG—balance of payments and reserves, 71, 74*; gold prices, 101*, 102

ICELAND—balance of payments and reserves, 76*; Fund quota, proposed increase in, 129*
INCOMES POLICIES—11, 44-45; *see also* individual countries
INDIA—balance of payments and reserves, 74*, 76*, 93-94; capital movements, 94; debt servicing problems, 94; economic policies, 78, 94, 110; Fund quota, proposed increase in, 129*; gold prices, 101-102; gold production, 96, 97; interest rates, 94; prices, 78, 93; ratio of taxes to national income, 22; surcharge on imports, 94, 110; transactions with Fund, 7, 94, 108*, 109*, 112*
INDONESIA—balance of payments and reserves, 74*, 76*; debt servicing problems, 29; Fund quota, proposed increase in, 129*; inflation, 78; monetary policies, 78; transaction with Fund, 109*
INDUSTRIAL COUNTRIES—3-4, 41-52; balance of payments and reserves, 4, 62*, 63-69; economic progress, 1950-64, 11; employment, 11; fiscal policies, 46-47; industrial production, 3, 41-44
INDUSTRIAL PRODUCTION—3-4; industrial countries, 41-44
INTER-AMERICAN DEVELOPMENT BANK—Fund cooperation with, 117
INTEREST RATES—41, 45, 46, 47, 48†, 49, 50; *see also* individual countries
INTERNATIONAL AND REGIONAL ORGANIZATIONS—Fund cooperation with, 117-18
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT—Fund cooperation with, 7, 8, 30, 117
INTERNATIONAL CAPITAL MOVEMENTS—4-6, 12-13, 50-52, 81; discouragement of, 5, 13, 46, 49, 52, 81, 85
INTERNATIONAL INDEBTEDNESS—*see* Debt Servicing Problems
INTERNATIONAL LIQUIDITY—14-19; conditional liquidity, 10, 14-15, 18-19; criteria for additional, 16; distribution of additions to, 17-18; and the Fund, 18-19; methods of creation, 16; potential insufficiency of, 8, 15; transferability, 16-17; unconditional liquidity, 14-15; *see also* Exchange Reserves; International Monetary System
INTERNATIONAL MONETARY FUND—*see* Fund
INTERNATIONAL MONETARY SYSTEM—8, 9-14; finance for deficits, 10; need for evolution, 15; place of gold, 15; swaps, 10, 14, 16, 46; *see also* Gold Exchange Standard; Gold Standard; Reserve Center Currencies
INTERNATIONAL TRADE—*see* World Trade
IRAN—balance of payments and reserves, 75, 76*; economic expansion, 75; Fund quota, proposed increases in, 32*, 129*; monetary policies, 78; transaction with Fund, 35, 108*
IRAQ—balance of payments and reserves, 75, 76*; Fund quota, increase in, 107, 108; Fund quota, proposed increase in, 129*; loan from Kuwait, 75
IRELAND—balance of payments and reserves, 76*; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increases in, 32*, 129*; transaction with Fund, 112*
ISRAEL—balance of payments and reserves, 76*; Fund quota, proposed increases in, 32*, 129*; monetary policies, 78; transactions with Fund, 35, 108*, 112*
ITALY—balance of payments and reserves, 3, 4, 42, 46, 60†, 64†, 65, 66, 67*, 68, 88-89; borrowing abroad, 46, 89; capital market, 51*, 52; capital movements, 61, 88*, 89; currency purchased by Fund with gold, 108*; currency used in Fund transactions, 112, 113*; economic expansion, 42; economic policies, 3, 89; exchange rate, 47†; exports and export markets, 42, 54, 58; fiscal policy, 47; Fund Article VIII, acceptance of, 107*; Fund quota, increase in, 108*; Fund quota, proposed increase in, 129*; General Arrangements to Borrow, 108*; gold and foreign exchange reserves, 69; gold prices, 58*; gold sales to U.S., 81, 99*; gross national product, increases in, 42*; industrial production, 3, 42, 43*; inflation, 85, 89; interest rates, 45, 49; monetary policy, 3, 46, 49, 89; prices, 3, 44, 57; transactions with Fund, 46, 112, 113*; wages, 3, 43
IVORY COAST—exports, 71; Fund quota, proposed increase in, 129*

JAMAICA—Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; transactions with Fund, 109*, 112*
JAPAN—balance of payments and reserves, 3, 60†, 64†, 65, 67*, 89-90; capital movements, 50, 60, 61*, 90; currency purchased by Fund with gold, 108*; currency used in Fund transactions, 35, 113; economic expansion, 3; economic policies, 3, 89; exports and export markets, 53, 55, 57, 58; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increases in, 32*, 129*; General Arrangements to Borrow, 108*; gold production, 96; industrial production, 3, 41†, 42; interest rates, 45, 46, 49; monetary policy, 3, 46, 49; prices, 44, 53*, 57; productivity, 43; transactions with Fund, 20, 109*; wages, 43†, 44
JORDAN—balance of payments and reserves, 76*; Fund quota, increase in, 107, 108; Fund quota, proposed increase in, 129*; transaction with Fund, 112*

KENYA—Fund quota, proposed increase in, 129*
KOREA—balance of payments and reserves, 76*; exchange rate, 36; Fund quota, proposed increase in, 129*; inflation, 78; monetary policies, 78; transaction with Fund, 35, 36, 109*, 110
KUWAIT—balance of payments and reserves, 73, 74*; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; loan to Iraq, 75

LAOS—Fund quota, proposed increase in, 129*
LATIN AMERICA—balance of payments and reserves, 67*, 71†, 75, 76*; debt servicing problems, 24*, 25, 26*; tax reforms, 22; *see also* individual countries
LEAD—72†
LEBANON—Fund quota, proposed increase in, 129*; gold prices, 101*
LIBERIA—debt servicing problems, 29; Fund quota, proposed increase in, 129*; transaction with Fund, 108*, 109*, 111
LIBYA—balance of payments and reserves, 76*; Fund quota, proposed increase in, 129*
LIQUIDITY—*see* International Liquidity
LUXEMBOURG—capital market, 51; Fund Article VIII, acceptance of, 107*; Fund quota, increase in, 107, 108*; Fund quota, proposed increase in, 129*; *see also* Belgium-Luxembourg

MALAGASY REPUBLIC—Fund quota, proposed increase in, 129*
MALAWI—membership in Fund, application for, 31
MALAYA—balance of payments and reserves, 74*; *see also* Malaysia
MALAYSIA—balance of payments and reserves, 75, 76*; Fund quota, increase in, 107, 108*; Fund quota, proposed increase in, 129*; transaction with Fund, 112*
MALI—exchange rate, 36; Fund quota, proposed increase in, 129*; monetary policies, 78; transactions with Fund, 35, 36, 108*, 109*, 110
MANUFACTURING COUNTRIES—balance of payments and reserves, 63*, 67*; exports, 53-60; *see also* Industrial Countries
MAURITANIA—Fund quota, proposed increase in, 129*; monetary policies, 78
MEXICO—balance of payments and reserves, 67*, 74*, 76*, 94*, 95; capital movements, 94-95; currency used in Fund transactions, 35, 113; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increases in, 32*, 129*; gold production, 96*, 97; gross national product, 95; prices, 95; public enterprises, 22-23
MONETARY POLICY—industrial countries, 45-46, 48-49; problems of, 12; successes of, 12
MONETARY RESERVES—of Fund members, reporting of and repurchases, 113-14; *see also* Reserves, Gold and Foreign Exchange
MOROCCO—balance of payments and reserves, 74*, 76*; Fund quota, proposed increase in, 129*; transaction with Fund, 35, 108*

NEPAL—Fund quota, proposed increase in, 129*
NETHERLANDS—balance of payments and reserves, 62*, 65, 67*; capital market, 51*; currency purchased by Fund with gold, 108*; currency used in Fund transactions, 35, 113; exports and export markets, 58; fiscal policy, 47; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; General Arrangements to Borrow, 108*; gold purchases from U.S., 99*; interest rates, 45, 46, 49†; monetary policy, 46; prices, 44, 57*; wages, 43, 44
NETHERLANDS ANTILLES—balance of payments and reserves, 76*
NEW ZEALAND—balance of payments and reserves, 59, 67*, 74*, 76*; exports and export markets, 59, 71; Fund quota, proposed increase in, 129*
NICARAGUA—balance of payments and reserves, 76*; Fund Article VIII, acceptance of, 31, 107; Fund quota, proposed increase in, 129*; gold production, 97; transactions with Fund, 108*, 109*, 112*
NIGER—Fund quota, proposed increase in, 129*
NIGERIA—balance of payments and reserves, 71, 74*, 76*; Fund quota, proposed increase in, 129*; monetary policies, 78
NORWAY—balance of payments and reserves, 63*, 67*; capital movements, 51*; exports and export markets, 54, 57, 58*; Fund quota, proposed increases in, 32*, 129*

OILSEEDS AND OILS—72†
ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT—Fund cooperation with, 117

PAKISTAN—balance of payments and reserves, 75, 76*, 110; Fund quota, proposed increase in, 129*; monetary policy, 75; transactions with Fund, 35, 75, 108*, 109*, 110
PANAMA—balance of payments and reserves, 76*; Fund Article VIII, acceptance of, 107*; Fund quota, increase in, 108*; Fund quota, proposed increase in, 129*; transaction with Fund, 35, 108*
PAR VALUES—*see* Fund Members *and* individual countries
PARAGUAY—balance of payments and reserves, 76*, 110; Fund quota, proposed increase in, 129*; transactions with Fund, 109*, 110, 112*
PERU—balance of payments and reserves, 71, 74*, 76*; debt servicing problems, 26†; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increase in, 129*; ratio of taxes to national income, 22; transactions with Fund, 109*, 111
PETROLEUM EXPORTERS—balance of payments and reserves, 73, 74*; prices, 53
PHILIPPINES—balance of payments and reserves, 74*, 76*; Fund quota, proposed increases in, 32*, 129*; gold production, 96; gold subsidy program, 102-103; monetary policies, 78; transactions with Fund, 109*, 111, 112*
PORTUGAL—balance of payments and reserves, 67*, 76*; Fund quota, proposed increase in, 129*
PRICES—adjustment of, difficult, 13; cost of living, 44†; in Europe, 6; in industrial countries, 6, 41-44; of exports, 44†, 53, 57*, 58; of imports, 44†; of metals and minerals, 7, 70, 71; of primary products, 6, 7, 20, 70-71, 72†, 75, 91, 92-93; wholesale, 44; *see also* individual countries
PRIMARY PRODUCING COUNTRIES—6-8, 11, 20-30, 53, 70-78; balance of payments and reserves, 4, 6, 7, 63*, 64†, 65, 66, 68†, 68*, 71-78; capital movements, 6, 25, 70, 77-78; credit expansion, 77-78; debt burden and debt renegotiation, 23-30; economic developments and policies, 78; exports, 53*, 54*, 58*; fiscal problems, 20-23; inflation, 20, 21, 24; prices of exports, 20, 53*, 70*; study of trade problems by UN, 7; terms of trade, 6-7, 70; wages, 21; *see also* individual countries
PRIMARY PRODUCTS—70-71; *see also* Prices *and* individual countries
PUBLIC ENTERPRISES—pricing problems, 23
PURCHASES OF CURRENCY—*see* Fund Transactions

QUOTAS OF FUND MEMBERS—*see* Fund Quotas

REPURCHASES OF CURRENCY—*see* Fund Members; Fund Transactions
RESERVE CENTER CURRENCIES—8, 9, 10, 13-14
RESERVES, GOLD AND FOREIGN EXCHANGE—8, 13-14, 68-69; composition, 68*; world's monetary gold holdings, 66, 69, 97-99; *see also* Monetary Reserves
RHODESIA—gold production, 96; gold subsidy program, 103
RHODESIA AND NYASALAND—balance of payments and reserves, 74*; *see also* Malawi; Rhodesia; Zambia
RICE—72†
RUBBER—72†, 75
RUBBER EXPORTING COUNTRIES—74*
RWANDA—Fund quota, proposed increase in, 129*

SAUDI ARABIA—balance of payments and reserves, 71, 74*, 75, 76*; Fund Article VIII, acceptance of, 107*; Fund quota, increase in, 107-108; Fund quota, proposed increase in, 129*
SECURITIES MARKETS—*see* Capital Markets
SENEGAL—Fund quota, proposed increase in, 129*
SIERRA LEONE—Fund quota, proposed increase in, 129*
SINGAPORE—balance of payments and reserves, 74*; *see also* Malaysia
SINO-SOVIET AREA—trade, *see* World Trade; *see also* U.S.S.R.
SOMALIA—balance of payments and reserves, 76*; Fund quota, proposed increase in, 129*; monetary policies, 78; transactions with Fund, 35, 108*, 109*, 111, 112*
SOUTH AFRICA—balance of payments and reserves, 59, 67*, 73, 74*, 76*; exports and export markets, 59; Fund quota, proposed increases in, 32*, 129*; gold exports to U.K., 101; gold production, 96; gold subsidy program, 102
SOVIET AREA—trade, *see* World Trade; *see also* U.S.S.R.
SPAIN—balance of payments and reserves, 67*, 71, 73, 74*, 75, 76*; capital movements, 73, 75; currency purchased by Fund with gold, 108*; currency used in Fund transactions, 113; Fund quota, proposed increases in, 32*, 129*; gold policy,

10?; gold purchases from U.S., 99*; inflation, 75
Stand-By Arrangements—*see* Fund Transactions
Sterling Area—balance of payments and reserves, 63*, 76*; *see also* United Kingdom
Sudan—balance of payments and reserves, 76*; Fund quota, increase in, 107, 108*; Fund quota, proposed increase in, 129*; transaction with Fund, 108*
Sugar—70, 71, 72†, 75
Sweden—balance of payments and reserves, 63*, 67*; currency purchased by Fund with gold, 108*; currency used in Fund transactions, 113; exports and export markets, 57, 58*; Fund Article VIII, acceptance of, 107*; Fund quota, proposed increases in, 32*, 129*; General Arrangements to Borrow, 108*; interest rates, 45, 46, 49; monetary policy, 46; prices, 57
Switzerland—association with Fund's General Arrangements to Borrow, 34, 35; balance of payments and reserves, 63*, 67*; capital market, 51*; exchange rates, 47†; exports and export markets, 58*; gold purchases from U.S., 99*; interest rates, 45, 46, 49†; monetary policy, 46-47; prices, 57
Syrian Arab Republic—balance of payments and reserves, 76*; Fund quota, increase in, 108; Fund quota, proposed increase in, 129*; transactions with Fund, 108*, 109*, 112*

Tanzania—Fund quota, proposed increase in, 129*; membership in Fund, 31
Tea—72†
Thailand—balance of payments and reserves, 71, 74*, 76*; Fund quota, increase in, 108; Fund quota, proposed increase in, 129*
Tin—72†
Togo—Fund quota, proposed increase in, 129*
Trade—*see* balance of payments of individual countries *and* World Trade
Trinidad and Tobago—Fund quota, proposed increase in, 129*; initial par value agreed, 107*
Tunisia—balance of payments and reserves, 76*, 111; Fund quota, increase in, 107, 108*; Fund quota, proposed increase in, 129*; initial par value agreed, 107*, 111; monetary policies, 78; stabilization measures, 111; transactions with Fund, 35, 108*, 109*, 111
Turkey—balance of payments and reserves, 76*; debt servicing problems, 29; Fund quota, proposed increase in, 129*; transactions with Fund, 108*, 109*, 111, 112*

Uganda—Fund quota, proposed increase in, 129*
U.S.S.R.—gold production, reserves, and sales, 69, 97, 98†, 101; trade, *see* World Trade
United Arab Republic—balance of payments and reserves, 73, 74*, 76*; Fund quota, proposed increase in, 129*; monetary policies, 78; transactions with Fund, 108*, 109*, 111, 112*
United Kingdom—aid from foreign monetary authorities, 4, 13, 47-48, 84; balance of payments and reserves, 3, 4-5, 48, 54, 59, 60†, 63, 64†, 65, 66, 67, 68, 69, 83-85; capital market, 51, 52; capital movements, 4, 60, 61, 63, 68, 83-84; claims on, 50†, 68*, 69; currency used in Fund transactions, 113*, 114*; currency used in international transactions, 9; debt management, 46; economic controls, 4, 48, 84, 85; economic expansion, 83; exchange controls, 84; exchange rates, 47†; exports and export markets, 4, 54, 55, 57-58, 59, 84; fiscal situation and policy, 4, 47, 48, 52, 84; Fund Article VIII, acceptance of, 107*; Fund holding of sterling, 112; Fund quota, proposed increase in, 129*; General Arrangements to Borrow, 108*; gold and foreign exchange reserves, 4, 50†, 68*, 69, 83*, 84; gold imports and exports, 101; gold market and prices, 99-101; gold sales to U.S., 81, 99*; gross national product, increases in, 42*; incomes policy, 43, 45, 85; industrial production, 3, 41†, 42, 43*, 84; interest rates, 4, 45, 46, 48, 49, 84, 85, 100; monetary policy, 46, 48-49, 85; National Board for Prices and Incomes, 45; National Economic Development Council, 45; National Incomes Commission, 45; prices, 44†, 57; sterling balances, 13; support for sterling, 4, 13, 47, 84-85; transactions with Fund, 4, 8, 20, 34, 35, 48, 84, 108*, 109*, 112, 113*; unemployment, 42; wages, 43, 44
United Kingdom Colonial Territories—balance of payments and reserves, 76*
United Nations—Conference on Trade and Development, 7, 118; Fund cooperation with, 36, 117, 118; Trade and Development Board, 7, 117
United States—balance of payments and reserves, 4, 5-6, 8, 12, 45, 51, 59, 60†, 63, 64†, 66, 67-68, 79-82; capital market, 5, 50, 51, 79; capital movements, 5, 12, 60, 61, 63, 79, 80-81; claims on, 13-14, 50†, 68*, 69; currency used in Fund transactions, 35, 113*, 114*; currency used in international transactions, 9, 10, 13-14; deficits financed, 13, 14; economic expansion, 3, 4, 41, 80; exchange rate, 47†; exports and export markets, 53, 55, 56, 57, 58, 59, 79; fiscal situation and policy, 46-47, 49; Fund Article VIII, acceptance of, 107*; Fund holding of dollars, 112; Fund quota, proposed increase in, 129*; General Arrangements to Borrow, 108*; gold and foreign exchange reserves, 68*, 69, 80*; gold held for account of others, 99; gold policy, 102; gold production, 96*, 97; gold purchases, 81, 99; gold sales, 79, 80*, 99; gross national product, increases in, 42*; industrial production, 41, 42, 43*; Interest Equalization Tax, 5, 13, 49, 51, 79, 81, 82, 85, 90; interest rates, 45-46, 49; monetary policy, 5, 46, 48; money market, 13; pressures on the dollar, 81; prices, 6, 13, 44, 53*, 57, 79; transactions with Fund, 20, 34, 35, 108*, 109*, 112, 113*; unemployment, 3, 41; wages, 43
Upper Volta—Fund quota, proposed increase in, 129*
Uruguay—balance of payments and reserves, 76*; debt servicing problems, 26†; Fund quota, proposed increase in, 129*; inflation, 78; monetary policies, 78

Venezuela—balance of payments and reserves, 67*, 74*, 76*; Fund quota, proposed increases in, 32*, 129*
Viet-Nam—balance of payments and reserves, 76*; Fund quota, proposed increase in, 129*

Wage Costs—industrial countries, 44; *see also* individual countries
Wages—industrial countries, 4, 41-44; *see also* individual countries
Wheat—72†, 91
Wool—72†, 91
World Reserves—*see* Reserves, Gold and Foreign Exchange
World Trade—3, 41, 53-68; direction, 53*, 54*

Yugoslavia—balance of payments and reserves, 74*, 76*; Fund quota, proposed increase in, 129*; transaction with Fund, 112*

Zambia—membership in Fund, application for, 31
Zinc—72†