Treasury and Federal Reserve Foreign Exchange Operations*

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During the past six months, the international financial system was again subjected to considerable buffeting, particularly during the first three weeks of July when speculation against sterling reached major proportions. The impact of these pressures was cushioned, however, by use of the Federal Reserve reciprocal currency network and other central bank credit arrangements which, in the case of sterling, provided the time needed by the British Government to plan and put into effect the sweeping corrective program announced on July 20. By late August, the sterling and other exchange markets had settled down to reasonably well-balanced and orderly trading but in an atmosphere of continuing anxiety.

Against this background of market uncertainty, the Federal Reserve broadened out earlier discussions of increases in several of the swap lines to negotiation of a general expansion of virtually the entire network. The general objective of these negotiations was to increase the reciprocal credit facilities available, both to the Federal Reserve and to its central bank partners, to levels well above the size of any routine drawings that might reasonably be expected and thus to create a broad margin of safety against any unforeseeable threats to international currency stability. As a result of these negotiations, the Federal Reserve swap network has been enlarged from $2.8 billion to $4.5 billion.

Partly due to the backwash of the speculative pressures on sterling and partly reflecting seasonal payments patterns, the Federal Reserve made several drawings on the reciprocal currency lines during July and August in order to absorb flows of dollars to certain continental European central banks. A total of $150 million equivalent of Swiss francs was drawn in July under the arrangements with the Swiss National Bank and the Bank for International Settlements (BIS); drawings also were made under the arrangements with the Netherlands Bank in the amount of $65 million equivalent, with the National Bank of Belgium for $30 million equivalent, and with the Bank of Italy for $225 million equivalent. In late August the entire

Table I

FEDERAL RESERVE RECIPROCAL CURRENCY ARRANGEMENTS AND COMMITMENTS

Institution	Amount of facility		System commitments
	February 28, 1966	September 15, 1966	August 31, 1966
	In millions of dollars equivalent		
Austrian National Bank	50	100	
National Bank of Belgium	100	150	20
Bank of Canada	250	500	
Bank of England	750	1,350	
Bank of France	100	100	
German Federal Bank	250	400	
Bank of Italy	450	600	
Bank of Japan	250	450	
Netherlands Bank	100	150	65
Bank of Sweden	50	100	
Swiss National Bank	150	200	75
Bank for International Settlements	300*	400*	75
Total	2,800	4,500	235

* Half is available in Swiss francs and half in other European currencies.

* This is the ninth in a series of reports by the Vice President in charge of the Foreign function of the Federal Reserve Bank of New York and Special Manager, System Open Market Account. The Bank acts as agent for both the Treasury and the Federal Reserve System in the conduct of foreign exchange operations.

Table II

OUTSTANDING UNITED STATES TREASURY SECURITIES FOREIGN CURRENCY SERIES

In millions of dollars equivalent

Issued to	Amount outstanding January 1, 1966	Redemptions—1966 I	II	July-August	Amount outstanding August 31, 1966
Austrian National Bank	100.7		— 25.2		75.5*
National Bank of Belgium	30.2				30.2
German Federal Bank	602.1	—100.6	—100.6	— 50.3	349.5
Bank of Italy	124.8				124.8
Swiss National Bank	257.3		— 23.2	— 23.0	211.1
Bank for International Settlements†	92.6				92.6
Total	1,207.8	—100.6	—148.9	— 73.3	883.8

Note: Discrepancies in amounts are due to valuation adjustments and rounding.
* $25.2 million equivalent redeemed September 6.
† Denominated in Swiss francs.

drawing on the Bank of Italy was repaid from a United States drawing of lire from the International Monetary Fund (IMF), and a repayment of $10 million was made on the drawing from the National Bank of Belgium. As of August 31, therefore, the total outstanding drawings by the Federal Reserve amounted to $235 million.

During the course of the late spring and summer months, the Bank of England drew on the swap line with the Federal Reserve, and $300 million remained outstanding as of August 31. With the increase in the Federal Reserve-Bank of England facility to $1,350 million, there thus remains available to Britain somewhat more than $1 billion of unused credit facilities under this arrangement. Moreover, on September 13 the Bank of England announced the negotiation of new facilities with other central banks. Apart from the new facilities the Bank of England still has at its disposal important unused facilities arranged previously. Finally, in August the BIS drew $75 million from the Federal Reserve under the reciprocal credit facility providing for drawings against European currencies other than Swiss francs.

In April and May, before the exchange markets became disturbed by flows of volatile funds, the United States Treasury also made further substantial progress in retiring outstanding obligations in the foreign currency series. Beginning in the summer of 1965, a good start had been made in repaying German mark-denominated obligations of the Treasury as the German balance of payments moved into deficit, and further progress continued through July 1 by which time the total mark obligations outstanding had been reduced from a peak of $679 million to $350 million. In addition, opportunities appeared to acquire Swiss francs and Austrian schillings, and repayments of $46 million of Swiss franc securities and $50 million of Austrian schilling securities were effected. As a result, such Treasury foreign currency obligations were reduced on balance by $400.2 million equivalent from the peak of $1,259.1 million in July 1965 to $858.9 million equivalent on September 6, 1966. Since the Treasury regards such foreign currency obligations only as a means of financing temporary balance-of-payments deficits, it naturally takes advantage of every market opportunity to retire such obligations at maturity or, in certain circumstances, to effect repayment in advance of maturity.

During the period under review, the Bank of Italy continued its cooperative efforts to minimize the impact on world financial markets of Italy's heavy balance-of-payments surplus. As previously noted, the Federal Reserve made drawings of $225 million in Italian lire on the swap line of the Bank of Italy in July and early August, and this swap drawing was liquidated in August. The lire needed to repay the Bank of Italy were acquired by a United States Treasury drawing of $250 million equivalent of lire from the IMF. In order to insure that the Fund's supply of lire would be adequate to finance such a United States drawing, the IMF, whose regular lira holdings were at a low level, arranged to borrow from Italy the lire needed for the United States drawing. This transaction was of material benefit to the United States and Italy and demonstrates the flexible manner in which the Fund can assist reserve currency countries as well as other countries in financing their balance-of-payments surpluses and deficits.

STERLING

Sterling enjoyed a six-month period of recovery, following the announcement of new international support for the pound on September 10, 1965. As dollars flowed back to the Bank of England between September and February 1966, the bank repaid in its entirety $890 million in short-term credit received from the Federal Reserve and the United States Treasury and, in addition, succeeded in liquidating a substantial part of its forward exchange commitments. Beginning in late February, however, sterling began to weaken once again, and by July the pressures had reached crisis proportions. Indeed, even when the British Government reacted to the massive attack on the pound by announcing on July 20 a profound and far-reaching austerity program, the exchange markets were so demoralized after two years of almost continuous tension that there was no immediate recovery in sterling. To be sure, the intense selling wave was stemmed, but market sentiment remained extremely cautious and after a brief upward surge the sterling rate again declined. By early September, however, there was evidence that the British Government's determination to defend sterling would receive broad public support and that the program was already beginning to show results.

At the end of February the sterling rate moved below par for the first time since September 1965, as the exchange markets became more cautious in view of the disappointing January trade results and the impending British general election scheduled for late March. These uncertainties were reflected particularly in a reduced volume of sterling trading and an increased vulnerability of the spot rate to any downward pressures. When the sterling rate dropped very sharply on March 9, to \$2.7930, the Federal Reserve entered the market with heavy bids for sterling. This reminder of continued United States official support quickly reassured the market, and sterling rebounded to about \$2.7960 on the following day. Over succeeding weeks, however, the pound again eased, as the uncertainties generated by the approaching election were reinforced by an increasing stringency in the Euro-dollar market—a development that was to intensify in coming months and exert recurrent pressure on sterling as funds flowed from London.

The Labor Party's decisive victory at the polls on March 30 produced little reaction in the exchange markets since this result had long been anticipated. Indeed, the markets remained relatively quiet throughout April, awaiting Chancellor Callaghan's new budget. When the budget was announced, however, the market interpreted it as being only moderately restrictive, with the principal provisions not taking effect until the fall, and initially there was some selling of sterling. With support from both the Bank of England and this Bank, the market soon regained its equilibrium, but it remained vulnerable to any new setbacks.

In this atmosphere, the outbreak of the British seamen's strike in mid-May was a devastating blow. Sterling quickly declined to about \$2.7900 in heavy trading and, as the strike dragged on, the market became increasingly apprehensive. The announcement of a large reserve decline in May heightened the general tension, and the first of a series of intensive and prolonged selling waves began on June 3. Relief from these pressures was provided temporarily by the announcement in mid-June that the short-term credits from European central banks which had formed part of the September 1965 arrangements in support of the pound had now been placed on a continuing basis, this time including French participation. The Federal Reserve and United States Treasury participation in the September 1965 arrangements continues to be available to the United Kingdom alongside these other facilities.

The respite for sterling provided by the announcement of this arrangement was short-lived, however, as increasing stringency in the Euro-dollar market left British interest rates not fully competitive, with consequent outflows from London in late June. While spot sterling came under pressure, forward sterling quotations narrowed and a sizable arbitrage incentive in favor of the United Kingdom developed in relation to short-term instruments in the New York market. Consequently, the Federal Reserve Bank of New York, with the agreement of the Bank of England, undertook market swap transactions in which, for System and Treasury accounts, it bought a total of \$66.6 million equivalent of sterling spot and sold it for delivery one-month forward. This operation both reduced the arbitrage incentive to shift funds from New York and at the same time eased exchange market pressures and bolstered spot sterling quotations.

As the maritime strike continued and the situation in Rhodesia remained unresolved, market sentiment steadily deteriorated. Despite a 9 per cent rise in exports in the five months prior to the outbreak of the strike, the United Kingdom's trade account had not improved significantly over the corresponding months of 1965 as import demand had remained abnormally high. Moreover, the figures released at the end of June indicated that in the preceding four months, British reserves had declined \$372 million, even after recourse to central bank assistance. In addition, uneasiness was heightened by evidence of dispute within the Labor Party over the proposed tightening of the incomes policy, an important element in the long-term resolution of Great Britain's payments difficulties. The resignation from the government of Mr. Frank Cousins, a veteran trade union leader, proved particularly disturbing to market confidence.

Selling pressures on sterling intensified, reaching very heavy proportions in mid-July. In the face of these sales, the Bank of England continued to provide firm support for the pound in both spot and forward markets, and on July 14 raised its discount rate from 6 per cent to 7 per cent and doubled the special deposits required of the London and Scottish banks. The market, however, shrugged off the bank rate increase as merely a technical adjustment to rising interest rate levels abroad. That same afternoon Prime Minister Wilson, in speaking to Parliament, confirmed that Britain was faced with a new financial crisis and warned that additional measures would be taken by the government. As tension mounted, sterling was heavily sold in both the spot and forward markets, but determined resistance by the Bank of England prevented the market situation from getting out of hand.

Against this background, the British Government on July 20 introduced a massive austerity program that called for a wage freeze, restraint on prices and dividends, additional taxes, reduced travel allowances, and further curbs on public expenditures both at home and overseas. The new program clearly strikes at the problem of excessive domestic demand and, given adequate time, should prove effective. Reflecting the confidence of the United States Government that the British program could accomplish its objectives, the Federal Reserve moved into the sterling market shortly after the British Government's announcement on July 20 in order to stem, and if possible reverse, the drain on the Bank of England's reserves. By July 22, the sterling rate had recovered from \$2.7866 immediately before announcement of the new program to a level above \$2.7900.

In the final week of July and the beginning of August, the sterling rate held fairly steady, but no vigorous recovery developed as the market waited to see whether the British Government would succeed in carrying through so drastic a program. Indeed, sterling remained vulnerable to downward pressures throughout the month of August and, as yields on dollar-denominated investments rose rapidly, exerting a strong pull on funds from London, the spot sterling rate declined to \$2.7880 while forward sterling discounts narrowed very sharply to under 1 per cent. Nevertheless, there is already evidence that the British Government's new program has begun to take hold at the same time that the measures introduced in the April budget are also taking effect. Even before the full effect of these corrective measures is felt, the technical position of sterling, which has been grossly oversold in recent months, should bring about a strong recovery of the sterling rate. In the meanwhile, with the reinforcement of the Bank of England's credit lines that has now taken place with the Federal Reserve and other central banks, the Bank clearly has ample resources to deal with any temporary speculative flurries that might otherwise impede the progress of recovery.

SWISS FRANC

The Swiss franc declined steadily during the first quarter of 1966 as a result of seasonal influences, sizable outflows of capital induced by easy monetary conditions in the Swiss market, rising Euro-dollar rates, and attractive yields on offshore United States corporate issues. In early March, when the Swiss franc fell to \$0.2304⅛, the Swiss National Bank sold dollars to moderate the rate decline and replenished its dollar holdings by selling Swiss francs to the Federal Reserve and United States Treasury.

From February through early April, the United States authorities bought a total of \$118 million equivalent of Swiss francs. With these francs, the Federal Reserve System fully repaid its \$40 million equivalent German mark-Swiss franc swap with the BIS, while the United States Treasury liquidated a similar swap for \$15 million equivalent (see this *Review*, March 1966). The System temporarily added \$46 million equivalent to its Swiss franc balances, simultaneously selling these Swiss francs forward to the Treasury for delivery on May 16 and July 20, on which dates the Treasury repaid at maturity two Swiss franc-denominated securities issued to the Swiss National Bank as fiscal agent for the Swiss Confederation. (These repayments reduced the amount of such commitments from \$349.9 million to \$303.7 million equivalent.) At the same time, the Treasury added \$17 million equivalent to its Swiss franc balances. In addition, the Treasury purchased \$18 million in gold from the Swiss authorities.

During April, monetary conditions in Switzerland tightened and the Swiss franc began to strengthen. When the rate reached its effective ceiling of \$0.2317½ in early May, the Swiss National Bank entered the market as a buyer of dollars for the first time since the beginning of the year. The franc remained at the ceiling in subsequent weeks as the Swiss banking community began to repatriate funds to meet midyear liquidity needs and as foreigners who had previously borrowed Swiss francs switched to less costly Euro-currencies, paying off their Swiss franc borrowings with outright purchases of francs. At the same time, mounting pressures on sterling added further to the demand for Swiss francs. Consequently, during May and June the Swiss National Bank took in \$200 million through outright purchases, and an additional \$82 million in short-term swaps with Swiss commercial banks to help provide for their temporary midyear requirements.

By July, uncertainties generated by the pressures on sterling again dominated the foreign exchange markets, and the usual reflux of funds from Switzerland following the midyear window-dressing date was sharply reduced. Moreover, as some additional funds gravitated to the country, the franc remained at or close to its ceiling. Accordingly, in July the Federal Reserve reactivated its swap facilities with the Swiss National Bank and with the BIS, drawing \$75 million of francs from each bank to absorb uncovered dollars from the Swiss central bank. In addition, the Swiss authorities purchased \$20 million of gold from the United States Treasury. Thereafter, however, pressures on sterling subsided somewhat, and with yields on dollar investments moving higher during late July and August, funds once more began to flow out of Switzerland, and the franc eased well below its ceiling.

GERMAN MARK

The deficit that had emerged in the German balance of payments during 1965 continued at a reduced rate in early 1966. In the first five months of this year official German reserves declined $310 million (exclusive of a payment on its increased IMF quota), reflecting short-term outflows of funds attracted by higher Euro-dollar rates, and rising net overseas expenditures for services. Consequently, during this period the mark was generally on offer at rates somewhat below the parity of $0.2500.

The ready availability of German marks enabled United States monetary authorities to continue purchasing marks —as they had since June 1965—in order to repay medium-term mark-denominated United States Treasury indebtedness to the German Federal Bank. By March 1, 1966 some $175 million equivalent of such obligations had been repaid (see this *Review*, March 1966). In the next four months a total of $117 million equivalent of marks was purchased for Treasury account, mostly in the New York market. The Treasury used these marks, together with balances on hand, to redeem at their respective maturities on April 1, June 1, and July 1 an additional $150 million equivalent of mark-denominated securities held by the German Federal Bank. Thus in the course of twelve months ended in mid-1966 the Treasury had reduced its mark-denominated indebtedness by $326 million to $350 million equivalent.

The German Federal Bank had been pursuing a generally more restrictive monetary policy throughout 1966, and on May 26, in line with this policy, it announced an increase in its discount rate to 5 per cent from 4 per cent. With large tax payments also falling due in June, the German money market tightened toward midyear. This factor, together with increasing pressures on sterling, the usual midyear window-dressing operations, and the beginnings of a recovery in the German trade position following a sharp deterioration in 1965, contributed to renewed demand for marks. By late June the spot mark had risen to parity. The further worsening in the sterling situation and the continued improvement in Germany's trade account imparted additional strength to the mark in July, and by the end of that month official German reserves were $391 million higher than at the end of May. More balanced conditions emerged in the exchanges in August, however, and mark quotations steadied at about $0.2506.

ITALIAN LIRA

Italy continued to register a substantial balance-of-payments surplus during the first eight months of 1966. The surplus was smaller than a year earlier, however, partly because of a wider trade deficit but mainly because of a sizable outflow of long-term capital attracted by the high yields available in the international bond market. In addition, Italian commercial banks once again began supplying fairly important amounts of short-term funds to the Euro-dollar market in the early months of the year. These short-term outflows offset the overall surplus and Italian official reserves actually changed little during the first half-year.

At the beginning of 1966, the Federal Reserve had outstanding a drawing of $100 million under its swap arrangement with the Bank of Italy. In February, this drawing was liquidated using $50 million equivalent of lire purchased in a special transaction with a foreign central bank and $50 million acquired through a sterling-lira swap with the BIS. In March and May, there were occasionally small offerings of lire in the New York market and the Federal Reserve purchased a total of $10 million equivalent. These lire were used on May 25 to reduce the third-currency swap with the BIS from $50 million to $40 million equivalent.

In June, demand for lire began to rise as Italy's tourist season moved into full swing. By this time, moreover, most Italian banks had already eliminated any net liability position vis-à-vis foreigners, and in these circumstances the Bank of Italy was no longer prepared to shift dollars abroad through short-term swaps with those commercial banks at preferential rates. As a result, the Italian payments surplus was increasingly reflected in the growth of official reserves, which rose rapidly during the summer months. Accordingly, the Federal Reserve reactivated its $450 million swap facility with the Bank of Italy in July and early August, absorbing a total of $225 million from the Italian authorities. These drawings under the swap arrangement were liquidated through a United States drawing of $250 million equivalent of lire from the IMF on August 22. The lire drawn from the Fund were sold by the United States Treasury to the Federal Reserve, which in turn used $225 million equivalent to repay in full its swap commitment to the Bank of Italy. The remaining $25 million equivalent, plus $1 million of existing lira balances, was used to reduce to $14 million the sterling-lira swap with the BIS. Federal Reserve and Treasury technical forward commitments in Italian lire, undertaken in 1965, remained unchanged during the period covered by this report.

BELGIAN FRANC

The Belgian franc traded below its ceiling during the first half of 1966, as the sizable current account surplus of the previous year gave way to a small deficit. In the late spring, however, as credit policy in Belgium tightened and the money market firmed, the spot franc rate began to strengthen. The National Bank of Belgium moved to reinforce its existing measures of restraint by raising its discount rate by ½ percentage point to 5¼ per cent on June 2. Nevertheless, official reserve gains remained small until July and August, when funds were repatriated as a result both of the domestic liquidity squeeze and the speculative pressure on sterling. The spot franc rate moved to its ceiling in late July, and the National Bank began purchasing fairly sizable amounts of dollars.

In order to absorb some of the rapid increase in Belgium's holdings of dollars, the Federal Reserve in August reactivated the $50 million standby portion of its $100 million swap facility with the National Bank of Belgium and purchased a total of $30 million from the Belgian authorities. Later in August, however, the Belgian money market eased and funds once again began flowing abroad in response to higher dollar investment rates. The National Bank then began supplying foreign exchange to the market and covering these losses by purchasing dollars from the Federal Reserve. Thus, by the end of the month the System was able to reduce its short position in Belgian francs to $20 million equivalent.

DUTCH GUILDER

The Dutch guilder was generally on offer during the first four months of the year, as both seasonal weakness and some special factors contributed to a widening in the Netherlands trade deficit. Occasionally, tight money market conditions in Amsterdam induced inflows of short-term funds which temporarily offset the downward pressure on the guilder rate, but on balance quotations eased noticeably. As early as January, the guilder was quoted below par, and by late April it had reached the lowest level since the revaluation of March 1961.

Effective May 2, the Netherlands Bank raised its discount rate to 5 per cent from 4½ per cent in order to curb the growth of domestic bank credit and stem the deterioration of the Dutch balance of payments. The guilder immediately rallied and then continued to rise, reaching par by early June. After midyear, increasingly tight money market conditions in Amsterdam and growing tensions in the sterling market led to a sizable inflow of funds. As a result, Dutch reserves increased $94 million in July and rose further in early August, and the Federal Reserve reactivated its $100 million swap facility with the Netherlands Bank, drawing a total of $65 million of guilders and using them, together with $2.5 million of guilder balances, to absorb an equivalent amount of dollars. By mid-August, however, the Dutch money market had eased and, as increasingly attractive interest rates on dollar investments were exerting a pull on Dutch funds, there was no further need for System operations in guilders.

AUSTRIAN SCHILLING

Austria's international reserves decreased in late 1965 and early 1966, as a consequence of a weakening in the Austrian balance of payments. In order to meet this development, the Austrian National Bank in April sold to the United States Treasury $25 million of Austrian schillings and the Treasury used these schillings to repay at maturity an Austrian schilling-denominated Treasury bond. Austria's overall payments position then improved, and through the early summer months the Austrian National Bank was able to add somewhat to its reserves. In late August, however, there was again an outflow of funds from Austria, and official reserves declined. Once again, this provided an opportunity for the Treasury to acquire Austrian schillings, and on September 6 the Treasury paid off another $25 million equivalent Austrian schilling-denominated bond, thereby reducing its total schilling-denominated indebtedness to $50 million equivalent.

CANADIAN DOLLAR

Movements in the Canadian dollar rate during the early months of the year were significantly influenced by fluctuations in the volume of new Canadian securities offerings in New York. At the same time, seasonal weakness in the trade account and Canadian government purchases of about $110 million of United States-held Canadian government debt resulted in a decline of $323 million in Canada's official gold and dollar reserves during the first half of the year (after payment of $47 million to the IMF in connection with its quota increase). About mid-June, however, the return of seasonal strength in Canada's external accounts, announcements of some fairly sizable new securities sales in New York, and conversions of sterling by Canadian exporters as the pound came under increased pressure, led to a firming of the Canadian dollar rate. Moreover, the announcement on June 20 of a new Canadian-Russian wheat agreement, providing for shipments to Russia of $740 million of wheat over three years, helped sustain market demand. Official reserves nevertheless declined once again because of additional official purchases on July 2 of $31 million of United States-held Canadian Treasury securities.

Canadian dollars also were actively sought in the forward market during much of the period as a result of covered conversions by Canadian banks of domestic time deposits into United States dollar investments. In early summer, this demand was reinforced by intermittent buying by grain interests and by exporters hedging future sterling receipts. The latter activity subsided later in August, however, when an easier tone also reappeared in the spot market, with quotations fluctuating narrowly just below $0.9300. There were no Federal Reserve or Treasury operations in Canadian dollars during the period except for those relating to IMF transactions described below.

OTHER CURRENCIES

There have been no official United States transactions in French francs, Japanese yen, or Swedish kronor this year.

INTERNATIONAL MONETARY FUND

During the period under review, the United States made two separate types of drawings on the IMF. The first, designated "technical", extended the practice initiated in February 1964 of obtaining currencies from the IMF for sale to other countries making repayments to the Fund (see this *Review*, October 1965, page 208, for a detailed explanation of this type of operation). The United States Treasury, between March and August, arranged for drawings totaling $300 million equivalent of Canadian dollars. Whereas earlier the facilities were drawn on in their entirety at their inception, under the current arrangements drawings are made periodically as needed.

The second type of drawing was of the more conventional type in which member countries obtain currencies for use directly in the financing of their international payments deficits. The United States first had recourse to the Fund in this manner in July 1965, when it made a multicurrency drawing equivalent to $300 million and used most of the drawing to fund earlier short-term credits. On August 22, 1966, the Treasury again went to the Fund for this purpose, drawing $250 million equivalent of Italian lire and subsequently selling the lire to the Federal Reserve for liquidation of its $225 million equivalent swap commitment to the Bank of Italy and a partial repayment of a sterling-lira swap with the BIS. The Fund, whose lira balances were at a low level, borrowed the required lire from the Italian government under an agreement lying outside the $6 billion General Arrangements to Borrow (G.A.B.). This was the first occasion on which the IMF had employed its authority under the articles of agreement to borrow needed currency from a member country other than under the G.A.B., and it marked another significant step in the evolution of the Fund credit machinery.

United States drawings from the Fund between February 1964 and August 1966 have totaled $1,532 million. At the same time, other countries have drawn dollars from the Fund, thereby reducing the Fund's holdings of dollars in excess of 75 per cent of the United States quota and thus reducing this country's repayment obligation to the Fund. Consequently, at the end of August 1966 net United States indebtedness to the Fund was only $893 million.

The vital role that the IMF plays in the international financial mechanism was greatly reinforced last February when a general Fund quota increase of 25 per cent or more, adopted in 1964 by the Governors of the Fund, became effective for 58 members who had accepted the proposal and whose combined quotas as of February 23, 1965 constituted the requisite two-thirds majority for approval. By August 31, an additional 32 members had submitted their ratification, and Fund resources had been increased from $16 billion to $20.6 billion, or close to the ultimate $21 billion target for the Fund's entire 104 nation membership. The quota increases must be paid to the Fund partly in a member's own currency and partly in gold. Such gold payments, however, have entailed gold losses for the two key currency countries, the United States and the United Kingdom, as other members have converted dollars and sterling into gold for payment of their gold subscription. In order to compensate for these losses, the quota increase arrangement provides that the Fund will deposit a total of up to $350 million of gold with the Federal Reserve Bank of New York and the Bank of England. Insofar as the United States is concerned, these compensating operations began in September 1965 and as of August 31 the Federal Reserve Bank of New York held for United States Treasury account $202.7 million of gold so deposited by the IMF. The gold is reflected in the Federal Reserve's statement of condition under "other assets" and the deposit liability under "other deposits".

GOLD MARKET DEVELOPMENTS

The price of gold in the London market has ranged between $35.11 and $35.1940 during the first eight

Table III

UNITED STATES NET MONETARY GOLD TRANSACTIONS WITH FOREIGN COUNTRIES AND INTERNATIONAL INSTITUTIONS*

January-June 1966

In millions of dollars at $35 per fine troy ounce; United States net sales (−), net purchases (+)

Country	First quarter	Second quarter
Canada	+ 100.0	+ 50.0
Colombia	+ 7.0	
France	− 102.8	− 220.7
Lebanon	− 10.8	
Switzerland	+ 7.0	+ 11.0
United Kingdom	− 19.0	− 7.2
All other	− 15.6	− 0.4
Net sales	− 34.0	− 167.3

Note: Because of rounding, figures do not necessarily add to totals.
* Not reflected in this table are United States monetary gold transactions with foreign countries mitigated through special deposits by the IMF.

months of this year, with upward pressures on the price predominating during much of the period. The underlying supply-demand relationship in the market has been quite different this year, however, from the same period a year ago when similar price pressures prevailed. Private demand for gold this year has remained well below last year's levels, no doubt reflecting in part the much more attractive interest yields this year as a result of tightening credit conditions in many countries. On the other hand, the supply of gold coming on the market has also been considerably reduced from last year, primarily because of the shift in South Africa's balance-of-payments position. Whereas during the first seven months of 1965 South African gold reserves declined by $213 million, adding roughly that much to the supplies available from new production for sale in London, during the same period this year South African gold reserves have increased by $250 million, with consequent reduction of the amount of new production available for sale. As a result of this swing in South Africa's payments position and reserves, therefore, there has been a temporary decline of about $500 million in gold coming on the London market from this source. Moreover, there have been no Russian sales of gold during the first eight months of this year. Over coming months there is a reasonable likelihood that the flow of gold to the London market will return to more normal levels.