Recent Changes in United States Silver Policy*

Following the emergence in the late fifties of an increasingly severe shortage of silver, United States silver policy has undergone a series of changes, which in effect provide for the demonctization of silver. For a brief period in the late fifties, the Treasury was able to accommodate market demands by sales of "free" silver, that is, its holdings of silver over and above the amount legally required as "backing" for outstanding silver certificates. By late 1961, however, it was clear that the Treasury could not continue to fill market demands and at the same time meet the nation's increasing coinage requirements. Accordingly, in November of that year, the Treasury moved to conserve its free silver stock by temporarily suspending sales of silver to the market. At the same time, and for the same purpose, it also began to retire silver certificates in the first of a series of moves toward the removal of certificates from the currency system. The Treasury found it necessary to reenter the silver market in 1963 to prevent hoarding of silver certificates and coin as the market price approached \$1.29 per ounce. At this price the silver content of the silver dollar equals its face value, as does the bullion equivalent of silver certificates.1 Then in June 1965 Congress authorized the substitution of copper and nickel for silver in dimes and quarters, and reduced the silver content of the half-dollar. This move substantially reduced the domestic use of silver for coinage, but the Treasury still had to stabilize the market price of silver until the amount of silverless coins was adequate to meet public needs. In acting as a residual source of supply for foreign as well as domestic buyers, the Treasury, in effect, stabilized prices in world markets. However, following a burst

of speculative purchases in May of this year, the Treasury discontinued sales of silver to buyers other than "legitimate domestic concerns" and simultaneously invoked its statutory authority to prohibit the melting and export of silver coins. By early July it became clear that the amount of clad coins was adequate to meet public needs, and on July 14 the Treasury halted sales of silver to domestic users at the fixed price of \$1.29 per ounce.

SOURCES AND USES OF SILVER

The changeover to a silverless coinage system as well as earlier changes in silver policy was dictated fundamentally by the development of a global imbalance between industrial and other demands for silver and available supplies. The absorption of silver for industrial uses in noncommunist countries rose from an estimated 240 million ounces in 1961 to almost 360 million ounces last year (see Table I), largely reflecting a tremendous increase in silver requirements for such uses as photographic film, electronic components, and batteries. Moreover, with the increase in population and widespread use of vending machines, the demand for coinage has increased enormously. In the early sixties, the amount of silver needed

Table I

FREE WORLD SILVER PRODUCTION AND CONSUMPTION
1961-66

In millions of ounces

Silver	1961	1962	1963	1964	1965	1966
Consumption:						•••
Industrial usage	240	259	261	304	347	357
Coinage	137	128	166	267	376	108
United States	56	77	112	203	320	54
Foreign	81	50	55	64	55	54
New production	203	209	215	211	215	231
Global deficit	173	177	213	361	507	233

Note: Because of rounding, figures do not necessarily add to totals.

Sources: Handy and Harman, Annual Reviews; Annual Reports of the Director of the Mint.

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¹The silver content of the standard silver dollar, as established by Congress in 1792, is 371.25 grains or 0.7734 of an ounce of pure silver and is thus equal to its face value when the price of silver is \$1.2929 per ounce. Silver certificates are also exchangeable for 0.7734 ounces of silver per dollar. The value of the silver content of dimes and quarters is the same as their face value at \$1.3838 per ounce.

Table II
UNITED STATES SILVER CONSUMPTION AND SOURCES OF SUPPLY
1961-66

In millions of ounces

Silver	1961	1962	1963	1964	1965	1966
ndustrial consumption	105.5 34.9	110.4 36.3	110.0 35.0	120.5 37.0	137.0 39.0	150.0 42.0
Difference	70.6	74.1	75.0	83.5	98.0	108.0
Add United States coinage	55.9 126.5	77.4 151.5	111.5 186.5	203.0 286.5	320.3 - 418.3	53.9 161.9
Accounted for by: Net commercial imports Lend-lease returns Decline in Treasury stock	- 9.1 - 10.4 - 129.5	63.3 8.3 94.4	- 32.5 184.0	55.7 — — 366.3	- 12.2 - - 414.4	22.3 209.4
Total accounted for	- 149.0	— 166.0	— 216.5	- 310.6	- 426.6	- 187.1
Discrepancy	- 22.5	- 14.5	- 30.0	- 24.1	- 8.3	- 25.2

Note: Because of rounding, figures do not necessarily add to totals.

Sources: Handy and Harman, Annual Reviews; Annual Reports of the Director of the Mint.

to satisfy the demand for coins in the United States grew very rapidly. Thus, despite a slight reduction in the use of silver for coinage abroad, Free World absorption of silver for coinage alone rose from 137 million ounces in 1961 to as much as 376 million ounces in 1965—the last full year before the changeover to cupro-nickel dimes and quarters in this country. Over the same period, Free World production of silver remained almost stationary and has averaged only 211 million ounces annually. Consequently, the overall deficit widened from about 170 million ounces in 1961 to as much as 507 million ounces in 1965. The gap narrowed considerably in 1966 with the reduction in the use of silver for coinage in the United States, but the imbalance between industrial consumption and new production remained very large.

The global deficits, as shown in Table I, provide a rough measure of the degree of disequilibrium that has developed in Frec World silver markets. However, they considerably overestimate the excess market demand, mainly because United States coinage requirements have been satisfied entirely by drawing on Treasury stocks rather than market sources. Moreover, new production has been supplemented from time to time through a variety of other sources—demonetized coin, liquidation of private holdings, and sizable sales by communist countries. While the indicated deficits cannot be interpreted literally as measures of excess demand, they do indicate some of the dimensions of the overall shortage.

In the United States, silver usage increased very rapidly in the early sixties mainly as a result of the accelerated production of coins (see Table II). Inclusive of coinage

requirements, total domestic usage almost tripled from 1961 to 1965, after having remained virtually unchanged during the fifties. Part of the resulting imbalance was met by net commercial imports and, for a while, by returns of lend-lease silver. By 1963 foreign countries had almost fully discharged their obligation to return such silver, and in 1964, after the Treasury had reentered the market as a residual source of supply, all the excess domestic demand and some foreign requirements as well were filled by Treasury sales of free (or nonmonetized) silver. Indeed, in 1964 the global deficit was almost exactly matched by a decline in Treasury silver holdings, and in subsequent years both the annual drain on Treasury silver and global deficits were roughly comparable in size. The decline in Treasury holdings, together with other sources of silver, was consistently larger than the indicated domestic deficit, which suggests that in each year there was net private domestic accumulation of silver.2 This steady buildup in private silver holdings represented, not only regular business inventory needs, but also precautionary and speculative buying which was particularly large in 1964, when an unprecedented rise in coin production focused attention

² This discrepancy, as shown in the final line in Table II, is measured by the difference between the indicated deficit and the amount accounted for by net imports, lend-lease returns, and changes in Treasury holdings. While this discrepancy contains residual errors and includes Treasury sales to Government agencies, it also provides a rough measure of changes in private domestic holdings of silver.

on the limited availability of silver for both industrial uses and coinage requirements. Although speculative pressures apparently subsided in 1965, inventory accumulation again increased considerably in 1966 and continued during the early months of this year.

TREASURY POLICY

In accommodating excess market demands, while at the same time increasing coin production, the Treasury's total holdings of silver were necessarily subject to a continuous drain. However, the only silver that the Treasury was legally authorized to sell consisted of its stock of free silver, that is, the portion of its total holdings that was not required to back silver certificates (see Table III). These stocks were accumulated under the silver purchase legislation of the thirties, which required the Treasury to support the market through purchases of newly mined domestic silver. During the early postwar period the Treasury continued to add to its holdings, but by the late fifties the combined requirements for coinage and industrial uses began to exceed world production by increasingly larger amounts. For a while the Treasury was able to fill the gap through sales of free silver at \$0.925 per ounce. However, in the fall of 1961, there was a burst of speculative purchases, which

Table III
COMPOSITION OF TREASURY SILVER

End of period	Outstanding	Silver stock			
	silver certificates	Total	Backing	Free	
	Millions of dollars	Mi سر	Millions of ounces		
1961: December	2,336.5	1,831.5	1,807.0	24.5	
1962: June	2,276.6	1,778,0	1.760.8	17.1	
December	2,214.0	1,728.1	1,712.3	15.8	
1963: June	2,126.4	1,658.3	1,644.5	13.8	
December	1,998.0	1,554.6	1,545.2	9.3	
1964: June	1,810.5	1.430.6	1,400.2	30,4	
December	1,347.6	1,192.6	1,042.2	150.3	
1965: June	888.8	982.6	687.4	295.2	
December	687.5	803.6	531.7	271.8	
1966: June	602.1	689.4	465.6	223.8	
December	568.8	594.3	440.0	154.3	
1967: March	558.4	531.7	431.9	99.9	
June	397.6*	442.5	307.5	135.1	

Note: Because of rounding, figures do not necessarily add to totals.

Source: United States Department of the Treasury, Daily Statement.

would have quickly exhausted the remaining holdings of free silver. Accordingly, on November 28, the Treasury temporarily suspended sales of free silver to the market.

At the same time, the President instructed the Treasury to obtain silver required for coinage through the retirement of five- and ten-dollar silver certificates—denominations for which a replacement was available in the form of Federal Reserve notes. The potential supply of silver immobilized as backing for certificates in these denominations amounted to about 400 million ounces, or almost one fourth of the Treasury's total holdings. Since the Federal Reserve System was not authorized to issue notes in denominations of less than five dollars, there was no substitute available for the replacement of one- and two-dollar certificates. The President announced that he would recommend legislation to permit the Federal Reserve to issue notes in smaller denominations as well. The enabling legislation was enacted in June 1963.

Within two weeks after the Treasury's withdrawal from the market in 1961, the price of silver rose to about \$1.05 per ounce but then moved slightly lower on profit taking. In August 1962, there was a renewed wave of speculative purchases. These purchases, together with increasing industrial and foreign coinage demands, resulted in a series of price increases that carried the quotation to almost \$1.21 by the year-end. During the first half of 1963 the price moved gradually upward, and by the summer had reached its monetary value of \$1.29 per ounce. The Treasury could not allow the price to rise much above that level, for at higher prices silver certificates would have gone to a premium and, in the process, disappeared from circulation. Moreover, prices above \$1.38 would have provided an incentive to recover silver from subsidiary coinage through melting.

The June 1963 legislation, which authorized the issue of one-dollar Federal Reserve notes, eliminated the threat of a diminishing supply of one-dollar bills and, at the same time, increased the availability of silver for use in coinage. Moreover, the mechanics of the redemption procedure assured the availability of silver bullion to the market at its monetary value. It was not necessary that silver certificates be presented physically in exchange for bullion. Substantial amounts of silver certificates were being retired each day. Anybody wishing to acquire bullion could tender other funds in a form satisfactory to the New York or San Francisco Federal Reserve Banks and request those banks to purchase an equivalent amount of silver certificates and exchange them for bullion. As bullion was released, an equivalent amount of certificates was retired. From July 1963 until August 1965, the rate of retirement of silver certificates exceeded the Treasury's bullion losses resulting

Reduced by \$150 million under legislation approved in June 1967. The Secretary of the Treasury has determined that this amount of silver certificates has been destroyed, irretrievably lost, or held in collections and will never be presented for redemption.

from market sales and use in coinage. Consequently, the amount of free silver rose in the face of a decline in the Treasury's total holdings. By August 1965, the Treasury had been able to accumulate a supply of unencumbered silver in excess of 300 million ounces. Thereafter, bullion losses began to exceed the rate of certificate retirements, and the amount of free silver steadily declined.

While the retirement of silver certificates provided the Treasury with free silver needed to accelerate coin production, it failed to provide a lasting solution to the coinage problem. To be sure, increased production had virtually climinated the shortage of silver coins by the end of 1965. However, in order to protect the existing silver coinage, it was necessary to continue to stabilize the market through silver bullion sales. For, if the Treasury had discontinued its sales, the price would have quickly risen above \$1.38, and in the process subsidiary silver coinage would have disappeared from circulation, as silver dollars already had. After exhaustive study, the Treasury recommended and Congress enacted the Coinage Act of June 1965, which authorized the production of silverless dimes and quarters and reduced the silver content of the half-dollar to 40 per cent. In order to hold the market price at the \$1.29 level and thereby assure an orderly transition to the new coinage system, the act extended the Treasury's authority to sell unobligated silver. Among other provisions, the act authorized the President to establish a Joint Commission on the Coinage which would make recommendations upon such matters as "the time and circumstances under which the United States should cease to maintain the price of silver".

The passage of the act enabled the Treasury to reduce substantially the use of silver in coinage. Despite the reduced use of silver in coinage, the Treasury's stocks continued to decline and by the end of 1966 had fallen to slightly less than 600 million ounces, of which 440 million were required as cover for \$569 million of outstanding certificates. In the early months of 1967, the return flow of certificates from the public to the Federal Reserve Banks dwindled to negligible amounts. A substantial part of the certificates reported as still outstanding was probably lost or destroyed and presumably will never be presented for redemption under any circumstances. However, some certificates had probably been withdrawn from circulation in anticipation of an increase in the market price of silver. In any event, the resultant slowdown in the rate of certificate retirement, coupled with increasing silver purchases from the Treasury, some of which were undoubtedly speculative in character, resulted in a further erosion of the supply of free silver.

During the first two weeks in May, in particular, there

was an unprecedented increase in purchases and orders for silver, mostly for export, which if unchecked would have quickly led to the exhaustion of the Treasury's supply of free silver. This, in turn, would have resulted in an immediate increase in the market price and imperiled the continued circulation of silver coinage at a time when the amount of clad coin was not yet considered sufficient to meet the country's needs. In order to assure the continued availability of silver to the domestic market, the Treasury on May 18 discontinued sales of silver to buyers other than "legitimate domestic concerns" and simultaneously invoked its statutory authority to prohibit the melting or export of silver coin. These steps effectively removed the Treasury as a source of supply for buyers overseas, but domestic demands remained very strong.

On June 24, the President signed legislation, authorizing the Treasury to write off a maximum of \$200 million of outstanding silver certificates deemed to have been lost or destroyed, or held in private collections, in the expectation that such certificates would never be presented for redemption or flowback to the Federal Reserve Banks for retirement. Under this legislation the Treasury has already written off \$150 million in certificates, thereby releasing 116 million ounces of silver previously immobilized. The bill also provided that holders of silver certificates would have one year from the date of enactment of the legislation to redeem certificates for silver. After this period, silver certificates would continue as legal tender—the purpose for which they were issued as currency—but with no special redemption privileges.

By mid-July, the mints had produced about 81/4 billion pieces of the new silverless dimes and quarters and, in the process, virtually duplicated the entire stock of silver dimes and quarters in circulation. Moreover, during the remainder of this year the production of coins is scheduled at a monthly rate of 300 million pieces, and this rate can be stepped up to 700 million pieces should the need arise. Even if some silver coins should begin to disappear, as silver dollars already have, the amount of clad coins in circulation and in inventory or in process of production is fully adequate to meet forsceable needs. In view of the success of the coinage program and continued heavy demands for silver from domestic buyers, the Treasury—acting on a recommendation of the Joint Commission on the Coinage -on Friday, July 14, decided to halt all sales of silver at its monetary value. The following Monday, the price of silver for spot delivery in the New York market was raised to \$1.78 per ounce, and by early August had increased to about \$1.85 per ounce. At these levels the silver content of subsidiary coins exceeds their face value, but the prohibition on melting, which carries severe penalties, remains in effect.

The Treasury has announced that it will sell about 2 million ounces of silver a week under a competitive scaled-bid procedure. At first these sales will be restricted to domestic users, but later on foreign buyers may also be allowed to bid. Since the Treasury has written off \$150 million of silver certificates, the amount of free silver available for market sales has been substantially increased. Indeed, the Treasury's stock of free silver, which now stands at approximately 110 million ounces, is about as large as the 1966 domestic imbalance between industrial

demands and new production. While Treasury sales will help substantially to alleviate the domestic shortage of silver, such sales will no longer be made at an artificially low price. The price of silver, like many other commodity prices, is now determined fundamentally by market forces. In June 1968, when the right to redeem silver certificates comes to an end, the demonetization of silver will in effect have been completed. While this process has resulted in a slight change in the composition and appearance of the nation's coins and currency, it has in no way affected their value as a means of payment.