

Only \$96 million of short-term capital left the country in 1959 and \$306 million in 1958.

Speculation provides the most plausible explanation of the large outflow of American gold in 1960, inasmuch as the balance of international payments of the United States was much stronger in 1960 than in 1959. The merchandise trade surplus was higher in 1960 than in 1959 by \$3.4 billion, net receipts on account of services were down by only \$300 million while capital outflow was \$1.5 billion higher. There was little change in the level of unilateral transfers in the form of military expenditures abroad and nonmilitary foreign aid. If it were not for speculation in gold it could be expected that the improvement in the international accounts would have reduced the payments deficit to a figure substantially less than the \$3.7 billion reached in 1959. Instead, it was reduced to only \$3.5 billion.

It seems probable that the reason for the substantial withdrawal of gold during the latter half of 1960 was the purchase of gold from the U.S. Treasury by the Bank of England to replenish the gold that it has been paying to those who have been exchanging dollars and other currencies for gold for speculative purposes. Those who believe that the United States is going to devalue the dollar have only to hold gold while selling dollars short outside the United States. Then, if devaluation comes they will realize the difference between the old and the appreciated value of gold as pure dollar profit. The fact that the United States stands ready to buy gold, as well as to sell it, at the fixed price of \$35 per ounce places a protective floor under such speculation.

Although the cessation of speculation in gold would not solve the balance of payments problem, it would at least render it soluble. As long as the drain on gold for purposes of speculation continues the problem is almost insoluble.

Several ways have been suggested to stop the speculative drain. One of them¹ would have the United States announce in advance that, although it will continue to sell gold freely at \$35 per ounce, it will reduce its minimum buying price by successive steps according to an announced schedule thus appreciating, rather than devaluing, the dollar in terms of gold. An even simpler way² would be for the United States to continue to redeem dollars in gold at \$35 per ounce (i.e., to continue selling gold) but to abandon the guarantee to buy it from foreigners at the minimum price of \$35 per ounce. The abolition of the fixed buying price would be opposed, of course, by foreign producers of gold. There would be nothing to prevent the United States, meanwhile, from buying gold from domestic mines at \$35 per ounce or any other price. Although it is important that the United States support the international value of the dollar in terms of gold, there seems to be little reason for the United States to continue to support the world price of gold in terms of dollars.

CONCLUSIONS

The fact that the United States has an adverse balance in its international payments is not a cause for alarm as far as the basic economic strength of the country is concerned. However, there is a serious problem with respect to gold and confidence in the dollar that cannot be ignored.

¹ Proposed by Prof. Fritz Machlup, of Princeton University.

² Proposed by Dr. William Blitiz.