

the statistics. The statistics show a decline rather than an increase. Is that correct?

Mr. KLOPSTOCK. It is not entirely correct. We have to look at investments not only by banks but also corporations. We have to put the figures together. If we do, we find in early 1961 the investments by both U.S. banks and corporations in British money market assets increased to \$208 million from \$44 million in March of the preceding year.

Later on during 1961 a substantial part of these investments were liquidated because the covered interest incentive to move funds to the United Kingdom declined. It was no longer profitable to any considerable extent to move funds on a covered basis to the United Kingdom.

In the case of Canada, there was also a decline during the second, third, and fourth quarters of 1961. But during the first quarter of 1961 there was a very substantial movement of American money into the Canadian money market. That is now taking place again.

We have to look not only at the interest rate differential, but also at the forward discount of sterling or the Canadian dollar in terms of U.S. dollars. Corporations only invest abroad if the covered interest rate incentive makes it profitable for them to go into foreign money markets.

Senator PROXMIRE. Let me ask you, Mr. Klopstock, because you are one of the few economists who appeared before us who argues, or has been able to document to any extent the argument, that interest rate differentials are important in international outflow. Many support the notion that you have, I don't know that you have it or not, that we should have higher interest rates at the present time. Do you advocate higher interest rates now, or I should say, a little tighter money policy, an increase in the money supply?

Mr. KLOPSTOCK. I do not wish to take a position on interest rate policies. I am merely analyzing the impact of rates on capital flows.

Senator PROXMIRE. Would you agree or disagree that a policy of monetary tightness, that is, not increasing the money supply as the gross national product increases, would tend to discourage borrowing for home purchasing, borrowing for consumption purchases? It would tend to slow down the economy in this particular area?

Mr. Humphrey, in his very excellent paper, says that it would be a miscarriage "to sacrifice \$30 billion of potential output for the sake of speedier elimination of a foreign deficit, which is so very small by comparison and is already diminishing."

A little further on he says, "I should resist choking off a couple of billion dollars of building construction with higher long-term rates."

I don't want to be unfair, but I think if the discussion of policies should have any practical meaning, we should bring it down to the tough decision we have to make in considering the argument for higher interest rates for international payments purposes, but it obviously doesn't mean that the economy can move ahead on the same drive on the domestic basis.

Would you concede that this is a balancing problem or do you think that interest rates are not very important domestically?

Mr. KLOPSTOCK. I do believe that interest rates exert an important influence on home construction. I believe there is general agreement they do.