

true improvement in the capital account, mainly through the sale of American securities to foreigners increased enormously.

Now, I will just go on to the reserve transactions balance. On the reserve transactions basis the principle explanation is that with the tight money position here, and with the flood of Euro dollars, American banks brought home much of the funds that were deposited with their branches in London. This can't go on. It helps in the exchange market right away, but it is a short period thing. In the long run we have to have a reasonable surplus, on the current account, on trade primarily, to enable us to finance what for the United States is its natural capital-exporting position, foreign investment by individuals and by companies that goes on without regard for what the surplus on current account is.

The balance of payments in the second quarter shows a reduction in the current account surplus and an equivalent improvement on the capital side. I am not quite ready to regard the improvement on the capital side as merely short run. I am going to go into that but first I would like to mention another thing. The U.S. balance-of-payments position is much more complicated than even a reasonably good interpretation of our balance-of-payments deficit would show. Because the truth of the matter is to get the U.S. balance-of-payments position you have to add the deficit of the United States to the surplus of Canada, because if Canada has a surplus, as it did, it is going to borrow less from us in the long run.

I would say that our real international payments position, despite the deterioration in our current account, looked more hopeful in the second quarter because of the strengthening of those countries which are so closely linked to the dollar that we are almost underwriters of their balance of payments, Canada and Japan. Similarly, in continental Europe, which were the great surplus countries, the surplus wasn't very great except in Germany.

Let me tell you why I want to be a little more cautious than Fritz without altogether disagreeing with him. There is no substitute for strong current account surplus of the United States. On the other hand, I really believe that our corporations—many of them, not all of them—overdid this business of investing abroad. I think there is reason to believe that the desire of American corporations to invest abroad has materially changed from what it was 2 and 3 years ago.

Mind you, once you get into the business of having affiliates abroad, there is a certain amount of investment you must do just to retain your market position. But if we look at the figures put out by the Commerce Department on prospective plant and equipment expenditures for direct investment abroad, what is striking is that the increase is so small that it will be more than accounted for and financed by the normal growth in capital consumption allowances—

Senator PROXMIRE. How much of that is the result of restraint of one kind or another by the Federal Government and how much of that is the result of this kind of decision which you imply is being made that they feel they perhaps have overinvested in the European and Japanese market and other areas for investments are not as attractive as they seem?

Mr. BERNSTEIN. I think in the voluntary program—this is before the present program—a very big part of it was due to a handful of