tion, and we certainly should not mind. Perhaps they would prefer not to let the dollar float without any limits, but they could arrange for upper and lower limits if they so desired.

These are the three attractive possibilities, but unfortunately there is a fourth possibility, which they could choose. They could say, "We shall keep the dollar rate fixed for current-account dollars. We shall devalue the dollar or leave it float if it originates from capital transactions." Such a multiple-rate system could be enforced only through foreign-exchange restrictions on their part. Such a raction would be deplorable. I wouldn't like it, but I would rather have other countries impose foreign-exchange restrictions than the United States. Hence, from our point of view, this reaction would still be preferable to our own program of restrictions.

Senator, I think I have exceeded the time that you have allotted me, and I can only hope that your questions will give me an opportunity to expatiate on some of these issues. I thank you very much for your attention.

(Professor Machlup's prepared statement follows:)

PREPARED STATEMENT OF DR. FRITZ MACHLUP

Mr. Chairman and Members of the Joint Economic Committee, you have invited me to present, in these hearings on the 1968 Economic Report, my views on the international position of the United States. I have accepted with pleasure and especially appreciate that you encouraged me to include in my testimony historical as well as analytical aspects.

THE THREE PROBLEMS

It has become customary to divide discussions of the international monetary situation into three problems: liquidity, confidence, and adjustments. All three have to do with international monetary reserves.

The problem of liquidity is concerned with the adequacy of the combined total of reserves held by all national monetary authorities and with the capacity of the international system to provide for sufficient annual increases in total reserves.

The problem of confidence is concerned with the danger that holders of monetary reserve assets alter the composition of their holdings and in the process destroy large parts of the existing reserves.

The problem of adjustment is concerned with the distribution of reserves among various countries and especially with the reversal of such imbalances of payments as would result in persistent losses of reserves in particular countries.

Experts have for years debated the relative importance of the three problems. My own view has been that they should all be taken care of at the same time. Our Government, regrettably, has insisted on giving priority to the problem of liquidity. A very neat solution has been found for it. The agreement signed in Rio de Janeiro last September provides for a novel, but well-designed mechanism for creating and distributing new reserves in the form of Special Drawing Rights. We hope that this agreement will be ratified soon and then activated without delay.

Unfortunately, there is some danger of considerable delay in its activation. Our own declarations of intentions have contributed to this danger in that we have repeatedly stated that the creation of new reserves can be postponed until we have solved our balance-of-payments problem. If this has seemed to be clever tactics in order to get other nations to negotiate on the contingent creation of additonal liquidity, it probably was poor strategy. For it is difficult and perhaps impossible to remove our payments deficit in the near future. Yet, postponing the activation of the new scheme for the creation of liquidity will make it more difficult to restore balance in international payments. We should have tried to negotiate on all aspects of international monetary arrangements so that we would not be fouled up now in this vicious circle.

The worst part of the vicious circle lies in the problem of confidence. Too many people believe that there will be a scarcity of gold and an abundance of