As we indicated in our most recent policy statement, equilibrium in our international accounts does not require the elimination of the deficit. Rather its size should be reduced to a level compatible with the willingness of the rest of the world to voluntarily maintain or to increase their dollar holdings in line with the need for world liquidity. The reduction in our balance-of-payments deficit by means of restrictions on international trade and capital movements is inconsistent with our objective of securing benefits of greater trade and investment.

Despite some improvement in the underlying balance-of-payments position in 1968 compared to 1967, the underlying 1968 deficit (which excludes special transactions which our Government has persuaded other governments to undertake in order to make the recorded result look better) was still on the order of $2.7 billion on a liquidity basis. One encouraging aspect of the 1968 result is the large foreign purchases of U.S. stocks and there is some reason to believe that this trend will continue. However, there was also an unusually large inflow of foreign capital influenced by high interest rates in the United States and by reduction of outstanding foreign loans by U.S. banks. We cannot rely on these factors to provide lasting relief to our balance of payments.

The most disturbing aspect of the 1968 result was the virtual disappearance of our traditionally large merchandise trade surplus from a level of $3.5 billion in 1967. Clearly this reversal is critical. It results in large measure from a surge of imports induced by the inflationary growth of demand to which we have referred earlier. It is interesting to note that the growth rate in exports in 1968 was 9.5 percent, substantially above the rate in 1967.

We do not share the views expressed in the report that restrictions imposed by the United States for balance-of-payments reasons have been helpful. While they may have afforded temporary relief, by now it is evident that the controls have not restored equilibrium in our international accounts. Further, what started as a few, temporary controls have now become a network of apparenly more permanent controls which are wasteful, inefficient, and undermine our avowed objectives of encouraging international trade and investment.

While the report does stress the need for a domestic stabilization program to assist in the achievement of balance-of-payments equilibrium, we believe that this is *the critical need.* A stabilization program to achieve high employment and stable prices would serve to improve the trade surplus and to insure maintenance of sufficient dollar holdings by foreigners to reduce the need for controls.

The Council report notes a number of proposals which have been advanced for changes in the present exchange rate adjustment mechanism. While a review of the adjustment mechanism may be useful, we share the Council's view that intensive study would be required before serious consideration could be given to the adoption of any of the proposals which have been put forward. Such intensive study should focus on the practical effects on trade and investment flows of any changes from the present system.