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THE PRICE OF GOLD

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THE PRICE OF GOLD

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I. INTRODUCTION

GOLD in the world today has many facets. The nostalgia for gold convertibility sometimes gives rise to the belief that the restoration of a full and automatic gold standard domestically and internationally would solve, in some undefinable but inexorable way, the problems of economic and social balance. At the other extreme, gold is held to be an anachronism—"a barbarous relic"—that fits in badly with the current trends of political and economic thought; and, accordingly, it is asserted, it should not have any official monetary function. I shall not deal here with the whole gold problem. To my mind it is its price aspect that calls at the present juncture for a thorough discussion from the angle of domestic and international monetary policies. Accordingly, I shall discuss, first, the limited significance of the prices at which gold is traded on the so-called free and black markets; secondly, the fundamental flaws in the case of the gold miners who seek to obtain a higher price for their product; and thirdly, the proposal sometimes advanced that an appreciation of the monetary gold price would provide a solution of the so-called dollar shortage. The appropriateness of the present world price of gold will then be reviewed in the light of the resolute opposition of the United States and the International Monetary Fund to a gold price rise.

However, prior to re-examining the arguments for a higher gold price, I ought to make clear what its advocates actually mean. They do not mean a mere rise in the local official gold prices in terms of non-dollar currencies, but a rise in the United States gold price that would be accompanied by a proportionate increase in gold prices of other countries. In actual fact, a substantial increase in official gold prices has taken place since the end of the war in those countries which have devalued their currencies. These local gold-price rises have of course been merely an incidental result of currency readjustments, but they have had marked domestic effects, especially on the position of the gold-mining industry in the devaluing countries. Nevertheless, the advocates of a higher gold price have by no means been satisfied by these in-

¹ The views the author expresses are personal and do not purport to reflect those of the Federal Reserve Bank of New York. This essay, in a slightly different form, was originally prepared for presentation at the Third Meeting of Experts of the Central Banks of the American Continent, Havana, Cuba, February 25-March 7, 1952.

creases. On the contrary, the agitation in some quarters for a higher United States dollar value for newly-produced gold and existing private hoards and official monetary stocks has, if anything, become more vocal since the readjustments of national currencies in terms of the United States dollar in 1949. Such an upward revision in the United States gold price, so runs the argument, could best be made under the guise of a proportionate rise in gold prices in all countries, including the United States, within the framework of the International Monetary Fund.²

II. THE LIMITED SIGNIFICANCE OF THE FREE AND BLACK MARKET GOLD PRICES

The limited significance of the market price of gold will first be discussed in the light of gold trading and gold hoarding in those areas of the world where private gold hoarding and internal trading in gold are legal or where the emotional and instinctive predilection for gold is so strong that legal prohibition of gold hoarding merely results in large-scale clandestine gold trading. However, all gold hoarding should not be regarded as necessarily speculative. In the Middle and Far East gold hoarding appears as part of the normal saving pattern of the people, and the popular demand for gold in these countries is therefore determined more by the level of incomes than by the anticipation of gold price changes. When prices of the goods produced in these countries are rising, as in recent years, the hoarding demand increases; when prices are low relative to the official domestic gold price, as after the devaluations of the early 'thirties, there is a wave of dishoarding. On the Continent of Europe and in some parts of the Americas, the hoarding appears essentially as a means of minimizing losses that are expected to result from political, economic, and social upheavals and the concomitant inflationary pressures and currency depreciations. Finally, along the routes of the international premium gold traffic, there are various centers where middlemen and speculators buy and sell gold in order to derive a profit from short-term fluctuations in the market price of gold—fluctuations that depend in turn largely on the actual and an-

² Under Article IV, Section 7 of the Articles of Agreement of the International Monetary Fund, the Fund, by a majority of the total voting power, may make uniform proportionate changes in the par values of the currencies of all members, provided each such change is approved by every member whose quota is 10 per cent or more of the total. Theoretically speaking, a unilateral rise in the United States dollar price of gold would likewise, of course, increase the dollar value of the existing monetary gold stocks and current gold output. But such a rise would be equivalent to a devaluation of the dollar—a proposition that is manifestly absurd. A rise in the United States dollar price of gold is therefore conceivable only within the framework of a multilateral increase in world gold prices, and these two terms may accordingly be used interchangeably.

anticipated changes in the gold supply and demand in those countries where gold is hoarded in large amounts. It is because the tide of gold hedging against monetary instability in some parts of the world has coincided with the tide of high commodity prices and incomes in other areas that the hoarding demand in recent years has been particularly intense.

The net absorption of gold into nonmonetary uses, i.e., the professions, arts, and industry, as well as private hoards, had apparently fallen to a low level by mid-1950, prior to the outbreak of hostilities in Korea.³ Since then, however, large amounts of gold have been again absorbed into nonmonetary uses.⁴ This high rate of gold absorption has reflected partly releases from official gold holdings for nonmonetary purposes, and partly the increased proportion of newly mined gold made available for such purposes, especially from South Africa, whose sales of nonmonetary gold at premium prices represented in 1951 some 40 per cent of its output. It was apparently because of this increased supply of gold for nonmonetary purposes, and perhaps also because the demand for gold was less insistent than, for instance, in the first three quarters of 1949, that premium prices were much lower in 1951 and in the early part of 1952 than before the 1949 currency readjustments. Indeed, at no time since the outbreak of the Korean hostilities have the prices at which gold is traded directly for United States dollars in the clandestine or open markets—prices whose limited significance will be pointed out in the next paragraph—returned to the high point of \$55 per fine ounce that had been reported in May 1949. By mid-1950, the quotations most frequently reported were in the neighborhood of \$36, or very close to the United States Treasury price, but following the outbreak of the Korean war, they rose sharply to a peak of about \$44 early in January 1951; by December 1951 the price had declined again to somewhat less than \$39, and by mid-May 1952 to about \$37.

Great care, however, should be taken not to read too much into these prices. There is no free market for gold coin or bullion in the United States. Gold prices that are said to be United States dollar prices of gold reflect transactions by speculators and traders in gold that is either located outside the United States or is merely shipped to the United States for refining prior to re-shipment abroad. These premiums in

³ Cf. International Monetary Fund, *Annual Report 1951*, p. 73.

⁴ In 1951 gold production outside the United States (and also exclusive of the USSR) may be estimated at about 770 million dollars. Of this amount, some 600 million dollars of gold either went into industrial uses or private holdings or was otherwise unaccounted for. In 1950 this unexplained residual amounted to 300-350 million dollars, out of an annual foreign gold output that was likewise about 770 million dollars. This residual largely reflects the absorption of gold into nonmonetary uses, but part of it may be explained also by the "disappearance", of gold into undisclosed official holdings.

terms of the United States dollar are explained partly by the cost of overcoming the hurdles that impede the flow of premium gold, and partly by the actual and anticipated changes in the gold supply and demand on the markets where gold is traded in terms of various local currencies.

Where gold is traded against local currencies, still wider and more erratic premiums over the official dollar price of gold apparently exist. The actual prices embodying these premiums are of course quoted in local, inconvertible currencies. Whenever they are converted into United States dollars, they are merely computed figures arrived at by converting the local currency price into dollars. For most local currency quotations, different dollar equivalents can be obtained by converting the local currency price at different exchange rates (black market, official market, free market, etc.) and it is often difficult or impossible to know which rate will give a realistic dollar equivalent. In the Middle and Far East, where gold premiums are highest, dollar transactions are relatively few and unimportant; hence the so-called Far Eastern dollar prices of gold, which are the highest ones extant, are especially lacking in realism so far as any relation to the dollar price of gold is concerned. In Western Europe, on the other hand, free or black market dollar transactions are of some importance; and when the respective rates are used to convert the local currency gold prices, the apparent dollar premiums are much smaller than in the East. In those instances where the seller of gold wishes to make an actual conversion of his local currency proceeds into dollars, and is able to do so (such conversions being as a rule prohibited by law), the conversion is ordinarily made through free or black markets at rates that are usually at a substantial discount from the official rates of exchange.

The gold premiums in free and black markets therefore reflect, in the first place, the cost of overcoming the restrictions that impede the flow of gold between countries, and within countries where internal trading is restricted. To an even larger extent, however, they also reflect the monetary habits of the population, the efficiency and stability of the local monetary system and of government finances, as well as the varying prospects of the national government. In their very essence, foreign gold prices are therefore a reflection of local conditions in various countries, and cannot be looked upon as an indication of the intrinsic value of the United States dollar.

III. THE PRODUCERS' CASE

The gold producers argue that in the face of rising mining costs the gold price is unduly low, first, because the prices of other metals and

commodities have increased considerably in the last fifteen years and, secondly, because higher gold prices prevail on the free and black gold markets. Since, on the other hand, the mining costs have risen, 'something should be done for the gold miners.'

The gold producers' argument that mining costs are high and the gold price low bears a close resemblance to the standard argument of all producers of price-controlled commodities. It is sometimes argued even by disinterested observers that the gold industry's case deserves as much attention as that of any other industry whose end-price is controlled by the government, and accordingly, it is asserted, the producers have a right to a price that covers the cost of production. This analogy rests on the assumption that gold is a commodity. However, gold is not primarily a commodity, but a monetary metal since its marketing and its price are determined not by market forces but by actions of governments. It is for monetary reasons that there is a fixed official gold price to which the national currencies are related directly or indirectly, the mutual links between currencies in turn reflecting their relation to gold. The price of gold in terms of any currency has therefore a monetary significance of great import, both domestically and internationally. Whether the fixed gold price continues to serve fully its purpose must accordingly be judged solely from the monetary viewpoint. Gold producers themselves, in electing to engage in the business of producing the world's primary monetary metal, must be prepared to accept both the windfalls and the risks of their very specialized type of industry.

It is appropriate to point out that the bulk of international gold transactions takes place at the price of \$35 per ounce at which the United States Treasury is willing to buy gold and other countries are ready to sell it, or vice versa. There is little reason to doubt that, over much of the period since 1934, the price available to gold producers would actually have been well below \$35 if the United States had not been maintaining this fixed purchase price. It is at this price that the United States was offered and actually acquired 14.5 billion dollars' worth of gold from 1934, the year of dollar devaluation, to the end of 1951. During those years, gold production outside the United States (excluding also the USSR) was worth about 14.3 billion dollars. The United States purchases of foreign gold from 1934 to the end of 1951 exceeded therefore the equivalent of the whole new gold production in the rest of the world. In the light of these official United States gold purchases from the rest of the world, the transactions in nonmonetary gold appear relatively insignificant in comparison with the official movements of monetary gold. Whether it is in the long-term interest of the gold producers to secure a steady market for gold at a stable price rather than to encourage highly erratic free markets is a consideration that the miners

themselves should carefully ponder under present-day circumstances. As already noted, by mid-1950, after the disturbances of the early post-war years, practically all newly mined gold began again to flow into official monetary reserves, and premium gold prices fell quite close to the official prices. The post-Korean gold disappearance into hoards and the resurgence of gold premiums must not obscure the long-run monetary position of gold. The post-Korean premium gold prices, which as noted above had already declined considerably by mid-May 1952, are no indication of what the official United States gold price should be.

In actual fact what matters, from the viewpoint of gold miners outside the United States, is not the United States gold price, but the price of gold in terms of their local currencies. Although the United States Treasury gold price has remained unchanged since 1934, the price actually received by foreign gold producers in their own local currencies has been considerably increased as the rates of exchange of various currencies have been lowered in terms of the United States dollar. The sterling price of gold increased by about 16 per cent in 1939, when the dollar value of sterling was reduced from slightly over \$4.68 to \$4.03, and again by 44 per cent in 1949 when the rate was lowered to \$2.80. Producers in other countries that devalued likewise benefited from their higher official gold prices. The rise in official gold prices in these currencies was, of course, only an incidental result of the currency readjustments, but since the countries that devalued in 1949 account together for some 80 per cent of the world gold output outside the USSR, the profitability of gold mining was generally enhanced, although in varying degree in different countries.⁵ However, the continuing rise in costs under the impact of world-wide inflation has offset to some extent the original benefits conferred on gold producers by the currency readjustments.

The second argument, namely that gold producers should receive a price high enough to cover their costs, likewise appears valid only so long as gold is regarded as a commodity, and not as a monetary metal—an assumption that has already been challenged in general terms. Some specific considerations seem, however, called for here. The very fact that the gold producers are caught between a fixed gold price and rising costs of production merely reflects the nature of risks inherent in the production of a monetary metal. Actually, the marginal producers in many countries have obtained some relief from rising costs by shifting from lower to higher-grade ores.⁶ They have also improved their tech-

⁵ In Canada, however, the effect of currency depreciation in September 1949 was only temporary since the price received for Canadian gold production declined again in October 1950 when a free exchange market was established and the Canadian dollar subsequently appreciated in terms of the United States dollar.

⁶ In the Union of South Africa, however, the gold mining industry took advantage

niques. However, the cost-price problem in the gold mining industry is by no means a new one. Under the nineteenth-century gold standard, the gold price was kept stable and the gold miners had to readjust their output to the variations in their costs. Indeed, the very way in which, at least in strict gold-standard theory, the changes in the gold supply were brought about by the variations in gold-mining costs was one of the essential mechanisms supposed to produce a stable price level. It is a matter of historical record that in the periods of rising prices prior to 1945 there never was any notable demand for an increase in the price of gold. The fixed price of gold that is basic to the monetary status of gold was fully respected.

Furthermore, in a number of foreign countries the gold producers' claim that they are unable to meet their rising costs has in actual fact received consideration in recent years, not for the sake of the gold industry itself, but because of the industry's importance for a country's balance of payments. In some countries, such as South Africa, the burden of taxation of mining profits was reduced in 1948; and it was only in 1951 that taxation was restored to the previous level in view of the changed position of the industry, as will be noted below. Another device for increasing the gold-mining receipts was the use of subsidies. When the 1949 currency readjustments increased the profit margins of the gold industry, Australia and Southern Rhodesia abolished the subsidy, but Canada, which devalued in 1949 to a much smaller extent than the sterling area countries and beginning in October 1950 let its dollar appreciate in terms of the United States dollar, continued its subsidy through 1951. Finally, the South African producers were allowed, beginning in 1949, to sell part of their output for nonmonetary purposes at premium prices, a procedure which brought additional revenue to the industry.⁷ In the latter part of 1951, following the re-interpretation of the International Monetary Fund's gold policy that will be discussed later, Canada, Southern Rhodesia, Australia, and other gold-producing countries likewise allowed the miners, on certain conditions,⁸ to sell part of their current output for nonmonetary uses at

of the higher gold price to process lower grades of ore. This was one of the reasons why gold output failed to rise after the 1949 devaluation.

⁷ The additional revenue from premium sales by the South African mines amounted to \$2 per ounce in the early part of 1951, but it declined toward the close of the year; in the second half of 1950 it amounted to roughly 70 cents.

⁸ In Southern Rhodesia and West Africa, premium sales were at first to be limited to about 40 per cent of current output—a purely arbitrary figure that corresponded to the proportion of newly mined gold that South Africa was selling for nonmonetary uses in mid-1951—but in April 1952 South Rhodesian and West African gold mines were allowed to sell the whole of their production in the free market. In Canada and in Australia, on the other hand, there was no specific limitation on the amount of gold the industry was allowed to sell at premium. In Canada, however, a further condition was

premium prices. However, with the free gold price at about \$37 per ounce, as in mid-May 1952, the margin of profitability offered by the premium market was rather narrow.

The currency readjustments of September 1949, tax relief, the subsidies, and premium sales have variously alleviated the profit-and-loss position of the gold-mining industry in many countries. However, they have not by any means restored the exceptionally high degree of prosperity that the industry enjoyed in the 'thirties after the United States dollar devaluation in 1934 had raised the price of gold to \$35 per ounce (an extremely remunerative level, given the relative cheapness of labor and capital in these years). It is a similar rise in the United States dollar price of gold, under the guise of a uniform proportionate increase in the official gold prices of all principal countries, that some spokesmen for the gold-mining industry seem to consider as the cure for its difficulties.

Altogether apart from the broad economic issues inherent in a uniform appreciation of gold that will be discussed later, it may be questioned whether a high priority in over-all economic policy should be given to gold production. Gold is not an armament metal, and this was indeed the reason why direct government restrictions were imposed during the last war on gold mining in Canada, the United States, and Australia in order to release manpower and other resources for the armed forces. Whether a special incentive should be given to gold production during the present international emergency is a problem that must therefore be examined not from the viewpoint of the gold industry itself, but rather from that of the international economic policies of the United States, the British Commonwealth of Nations, Continental Western Europe and its overseas territories and Latin America.

IV. THE INTERNATIONAL LIQUIDITY ARGUMENT

The third line of approach put forward in recent years has been that the world price of gold should be raised for the sake of ensuring international liquidity. This argument has been made in two forms, one presenting world gold appreciation as a desirable instrument of monetary policy and the other treating it openly as a matter of sheer expediency.

In terms of monetary policy, the case for an upward revaluation of

established, namely that producers who sold gold in premium markets did so without subsidies; such subsidies were provided for in 1947 under a temporary legislation that was gradually extended (for the last time in December 1951 for another two years). In Canada, as well as in Australia, Southern Rhodesia, and West Africa, the sales were to be made against payment in United States dollars; in South Africa the payment of premiums, but not of the official dollar gold-price equivalent, was accepted in currencies other than United States dollars.

the world gold price⁹ starts from the assumption that gold is the only real money and that in view of the wartime and postwar increase in nominal money incomes and bank credit all over the world, the "measure of gold" should be changed in order to restore a proper proportion between the "cash" of each country—i.e. gold—and its money supply and external liabilities. If the "measure" is not properly adjusted, it is held, a worldwide deflation will ensue, as after the First World War.¹⁰ Both domestic and international liquidity are thus identified with gold, the only real medium of payment, and the only way of increasing them is to raise the world price of gold.

However, this metallistic concept of money, which treats gold as the only real medium of exchange in domestic as well as in international trade, appears an exceedingly narrow one in the light of the modern economic history of the Western world. Both common observation and economic analysis suggest, on the contrary, that money is generally defined by its acceptability, which in turn is not necessarily related to gold as the ultimate means of payment. Without discussing in this context whether final payments can be made only in goods, actual experience shows that final payments in international trade were made even under the 19th century gold standard through a complicated network of credit arrangements in sterling;¹¹ and under the gold standard as it existed just before the outbreak of the Second World War, the acceptability of sterling, which even then was the principal international medium of payment, was entirely divorced from the convertibility into gold at a fixed rate, as the whole history of the sterling area clearly illustrates.

⁹ Cf. W. J. Busschau, *The Measure of Gold*, Central News Agency Ltd., South Africa, 1949, 162 pages. *The South African Journal of Economics* published last year a series of articles dealing with the gold problem generally and with its price aspect in particular: W. J. Busschau, "Keynesian Views on the Price of Gold" (March 1951); C. Rist, "Gold and the Return to the Ideas of John Law" (March 1951); P. F. D. Wallis, "The Price of Gold and its Place in Monetary Theory" (March 1951); J. E. Holloway, "The Debacle of Money" (June 1951); Sheila van der Horst, "The Price of Gold: a Comment" (September 1951); Colin Bruce, "The Gold Controversy—a Comment" (December 1951); and W. J. Busschau, "Dr. van der Horst and the Price of Gold—a Rejoinder" (December 1951). Cf. also Harry G. Johnson, "The Case for Increasing the Price of Gold in Terms of all Currencies: A Contrary View," *Canadian Journal of Economics and Political Science*, May 1950, and his review of "The Measure of Gold" by W. J. Busschau, *The Economic Journal*, September 1950.

¹⁰ Cf. W. J. Busschau, *The Measure of Gold*, page 6: "The case submitted here is, in its simplest form, that because of the growth in incomes and credit (particularly long term obligations), increases in gold prices are necessary in order to obtain that degree of banking liquidity which will ensure the maintenance throughout the world of high levels of incomes and employment and that failure to increase gold prices sufficiently and in time will lead, as did the similar failure after World War I, to a severe credit deflation with its inevitable consequences of widespread unemployment and human misery."

¹¹ Cf. Roy F. Harrod, "The Pound Sterling," *Essays in International Finance*, No. 13, February 1952, International Finance Section, Princeton University.

Since the Second World War, it is the United States dollar that is widely sought, not for conversion into gold, but as an international means of exchange. Whenever settlements between countries other than those of the dollar area are effected in gold, it is an open question to what degree the recipient country accepts gold as such, in contrast to the attractiveness of the dollar-spending power that gold will provide when resold to the United States. The reason why the United States dollar is sought by other countries appears, in the final analysis, to be the ability of the United States economy to produce—more abundantly, promptly, and cheaply than any other country—many of the goods that the world needs. Conversely, the current difficulties of sterling as an international currency reflect in general not the lack of gold as such but Great Britain's inability, despite a considerable rise in its exports, to meet fully the sterling area's demand for imports, and the resulting need by that area to import goods from the United States.

The second comment called for by the international-liquidity case for a higher world gold price is that it is by no means certain that a mere increase in liquidity would make any direct contribution to the resolving of the world's current economic difficulties. Indeed, the case itself seems to rest principally on an analogy with the late 'twenties when the Gold Delegation of the League of Nations feared a world gold shortage. It appears in retrospect that the emphasis placed in the 'thirties upon international liquidity was overstated and that, on the other hand, the structural problems of the world economy were not adequately appraised. Recent experience points likewise to the conclusion that the fundamental need today is for a realistic step-by-step approach everywhere to necessary structural readjustments in productive capacity within countries and in the patterns of trade among countries, rather than a further dosage of cheap money and greater liquidity. It is up to each individual country to establish conditions conducive to higher economic productivity and greater monetary stability. The United States, through its technical know-how and selective financial aid, is willing to help—and is doing so on an increasing scale—individual countries in their determined efforts to produce more and better goods, and to create internal monetary and fiscal stability and a reasonable international balance. Such a determined approach to the basic economic and financial problems is more likely to bear fruit if the further disturbance to international values resulting from a rise in the world gold price can be avoided.

A higher gold price is also sometimes regarded as a first step towards the restoration of convertibility of currencies. Some writers believe that a world gold price rise would, in an undefined but seemingly inevitable way, not only help to re-establish the gold standard but also create the

necessary conditions for its maintenance. To my mind a gradual return to currency convertibility and its maintenance requires, in the short run, a reasonable monetary stability, and in the long run, sustainable production and trade patterns, of the "key" countries. The roots of the present currency disorder run much deeper than the apparent lack of international liquidity.¹²

The case for higher international liquidity has, however, been made also on grounds of sheer expediency, in the belief that an upward revision in the world gold price would add considerably to the easing of the so-called dollar shortage. The increase in the amount of United States dollars that the rest of the world gets from sales of gold to the United States either from current production or from monetary reserves would, it is asserted, considerably improve its balance-of-payments position. It is sometimes added that this process would be beneficial for the United States itself as it would make it possible for the United States to extend aid to foreign countries in a painless way, without any cost to the American taxpayer. This last point will be discussed in the next section.

As a starting point, the argument is usually put forward that the total monetary reserves of countries other than the United States are now much smaller in relation to foreign trade than before the war. At the end of 1951, those countries' total gold and dollar holdings, both official and private, were only 31 per cent higher than at the end of 1937. But their total imports, measured in dollars, have recently been running at an annual rate two-and-a-half times as great as in 1937, largely because of the rise in commodity prices. The monetary reserves of countries other than the United States are thus able to serve, it is stated, as a buffer only against relatively much smaller fluctuations in trade. Yet the need now is held to be for larger reserves than in the late 'thirties, partly because governments cannot reduce imports by allowing employment and incomes to fall, and partly because capital movements fail to flow in the equilibrating way they once did. The conclusion is thus reached that, as a remedial measure, the world gold price should be revised upward.

To this contention the same rejoinder must first be made as has already been put forward above, namely that the current problems of international trade appear to be more those of structural readjustment than of the lack of international liquidity. The added dollars that would be injected into the monetary reserves of other countries through a rise in the United States gold price would soon be dissipated if the serious unbalance in the foreign trade positions of those countries were not cor-

¹² For a bird's-eye view of the disintegration of the gold standard, see C. O. Hardy-M. A. Kriz, "The Gold Standard," *Encyclopedia Americana*, 1950 edition.

rected through measures aimed directly at the problem. Secondly, the contention that the gold price should follow commodity prices rests on the assumption that gold itself is a commodity and not a monetary metal—an assumption that, as already pointed out, is inadmissible. Thirdly, the argument that the increase in the prices of internationally traded commodities should be offset by a gold price rise is statistically less convincing than it superficially appears. The basis of comparison on which the argument rests is the assumption that in 1937 the United States gold price was, on the whole, in harmony with commodity prices. Yet this is a quite arbitrary assumption since by 1937 commodity prices had risen relatively little from the levels of the early 'thirties, while the United States gold price had increased 69 per cent. If an earlier year is taken as a basis, the result obtained is different. For instance, it is interesting to note that wholesale prices in the United States at the end of December 1951 were 78 per cent above the 1926 level, as against the 69 per cent rise in the United States gold price. The statistical argument, to say the least, is inconclusive.¹⁹ It may also be recalled in this context that the rise in the dollar price of gold that was brought about by the 1934 devaluation was designed to raise prices in general. The current agitation for a higher gold price aims, on the contrary, at raising that price alone. Insofar as there is any analogy whatever between 1934 and today it might be argued that the price of gold should be lowered, not raised, since one of the general world problems is inflation and further price increases should be prevented rather than encouraged.

Another pertinent objection against the world gold price rise as a remedial measure to the dollar shortage is that the benefits of a higher gold price would be quite uneven. Countries with low gold reserves would gain little; those with large reserves, as well as the principal gold-producing countries (Russia particularly) would gain disproportionately. However, even on optimistic assumptions as to the degree of upward revision in the gold price and the eventual rise in gold output, the resulting dollar increment would by no means be large enough to "solve" the dollar shortage. These considerations will now be examined in further detail.

World gold production (excluding the USSR) in 1951 may be estimated at some 24.1 million ounces, as may be seen from Table I and more fully from the chart on page 14. Of the world output, United States production amounted to 2 million ounces. Gold production in the rest of the world can therefore be put at 22.1 million ounces or 774

¹⁹ A still different result can be obtained by taking 1913 as a base. The official South African (and sterling) gold price between 1913 and 1950 rose 192 per cent, while commodity prices in the South African Union rose 106 per cent. The working costs of the South African gold mines rose 65 per cent. (Cf. Sheila T. van der Horst, "The Price of Gold: a Comment," *The South African Journal of Economics*, September 1951, pages 274 and 277.)

TABLE I
WORLD GOLD PRODUCTION
(In millions of fine ounces)

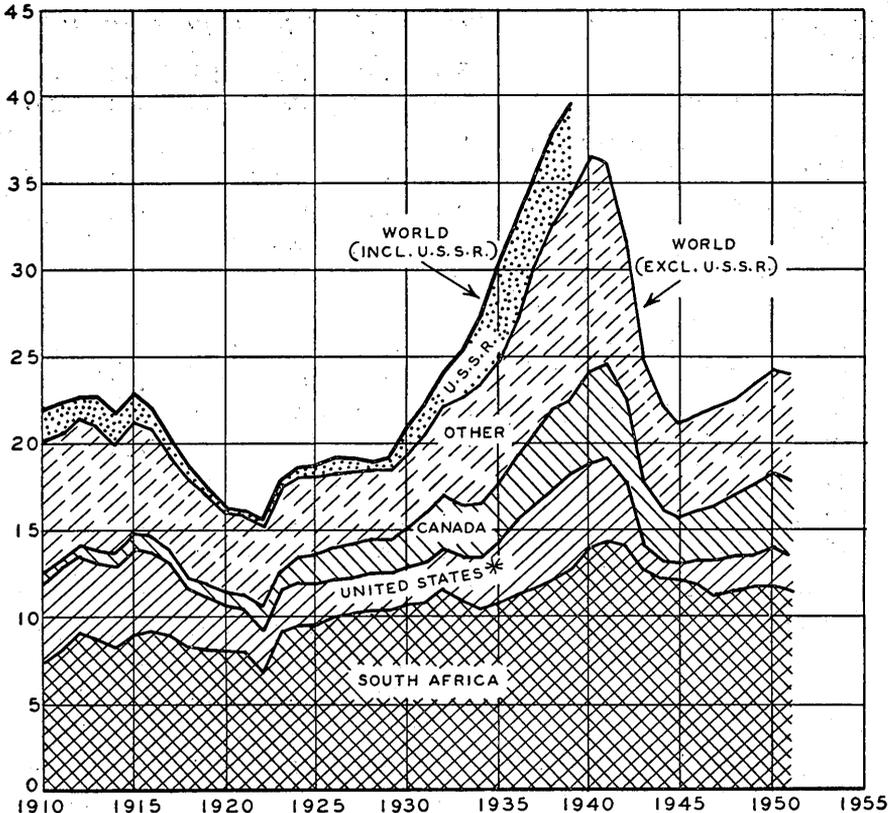
	1940	1947	1948	1949	1950	1951
North America:						
Canada	5.3	3.1	3.5	4.1	4.4	4.4
United States	4.9	2.2	2.0	1.9	2.3	2.0
Central and South America:						
Mexico	0.9	0.5	0.4	0.4	0.4	0.4
Colombia	0.6	0.4	0.3	0.4	0.4	0.5
Chile	0.3	0.2	0.2	0.2	0.2	0.2
Nicaragua	0.2	0.2	0.2	0.2	0.2	0.3
Africa:						
Union of South Africa	14.0	11.2	11.6	11.7	11.7	11.5
Gold Coast	0.9	0.6	0.7	0.7	0.7	0.7
Southern Rhodesia	0.8	0.5	0.5	0.5	0.5	0.5
Belgian Congo	0.6	0.3	0.3	0.3	0.3	0.4
Asia:						
India	0.3	0.2	0.2	0.2	0.2	0.2
Philippines	1.1	0.1	0.2	0.3	0.3	0.4
Oceania:						
Australia	1.6	0.9	0.9	0.9	0.9	0.9
Total	31.6	20.2	21.0	21.8	22.5	22.3
Other countries, excluding USSR	5.1	1.9	1.6	1.8	1.7	1.7
World, excluding USSR	36.7	22.1	22.6	23.5	24.3	24.1

Note: Figures may not add up to totals because of rounding.

million U.S. dollars at \$35 per ounce. If, for purposes of illustration, the production is valued at \$44 per ounce, which is an unrealistically high figure that has no significance whatever except that as being the post-Korean free-market peak, it would be worth about 972 million dollars. Let us further assume, for the sake of argument, that world gold output would increase in a few years under the impact of the higher gold price, as it did after the devaluations of the 'thirties, and that the output of 1940, which was an all-time record, would ultimately be reached again. As may be seen from Table I, gold output outside the United States in 1940 was 31.8 million ounces, or 1,113 million dollars at \$35 per ounce; at \$44 per ounce the hypothetical figure would

WORLD OUTPUT OF GOLD
(In millions of fine ounces)

MILLIONS OF FINE OUNCES



* Including Philippines through 1939.

be 1,399 million. Accordingly, on the basis of these two assumptions, namely the hypothetical price of \$44 and the ultimate attainment of the 1940 output, the value of newly mined gold outside the United States would increase from 774 million dollars in 1951, at \$35 per ounce, to a hypothetical figure of 1,399 million dollars some years hence. Out of this hypothetical increment of 625 million dollars, based on particularly favorable assumptions, only a part would of course be available for export to the United States; but even if it were available in its entirety, the ultimate contribution to the alleviation of the dollar shortage would indeed be small—particularly if the rise in the gold price, and the resulting impetus to cheap money, should result in further general price increases.

Thus far, only the aggregates have been considered. It should be also noted that gold production, as shown in Table I, is very unevenly distributed among continents and among countries. Gold is predominantly a sterling area product since about 60 per cent of world production (excluding the USSR) originates in that area. To the extent that gold flows to the British monetary authorities under the sterling-area pooling arrangements, pressure on Great Britain's dollar balance of payments—as distinct from its over-all balance of payments—would be lessened. On the other hand, Continental Europe would receive only negligible relief, with the exception of the Belgian monetary area which includes the Congo. The Soviet Union, which apparently is the second largest producer of gold (although its output is a matter of conjecture only), would automatically profit from a measure ostensibly designed by its proponents to benefit the Western world.

No less small and unevenly distributed would be the increment that the advocates of a higher gold price expect to derive from the existing monetary gold stock. An indication of the magnitudes involved can be derived from Table II showing world monetary reserves, while the accompanying chart provides a fuller background. The revaluation of the United States gold stock would itself, of course, be of no help to the rest of the world, unless it is suggested that the bookkeeping profit be "redistributed"—a suggestion that appears to take into account neither political realities nor the inflationary effects of revaluing gold under conditions of full employment coupled with rearmament. Should the estimated gold holdings of all other countries as of December 1951 be revalued at \$44 per ounce, the increment would be some 2.9 billion dollars. This potential accretion to foreign countries of United States

TABLE II

WORLD MONETARY GOLD RESERVES

(In billions of dollars)

	Dec. 1945	Sept. 1949	Dec. 1950	June 1951	Dec. 1951 ^p
United States	20.1	24.7	22.8	21.9	22.9
All other countries ^a	13.7	9.0	11.4	12.3	11.4
International institutions ^b	—	1.5	1.6	1.7	1.6
World ^a	33.8	35.3	35.8	35.9	35.9

^p Preliminary.

^a Excluding USSR; partly estimated.

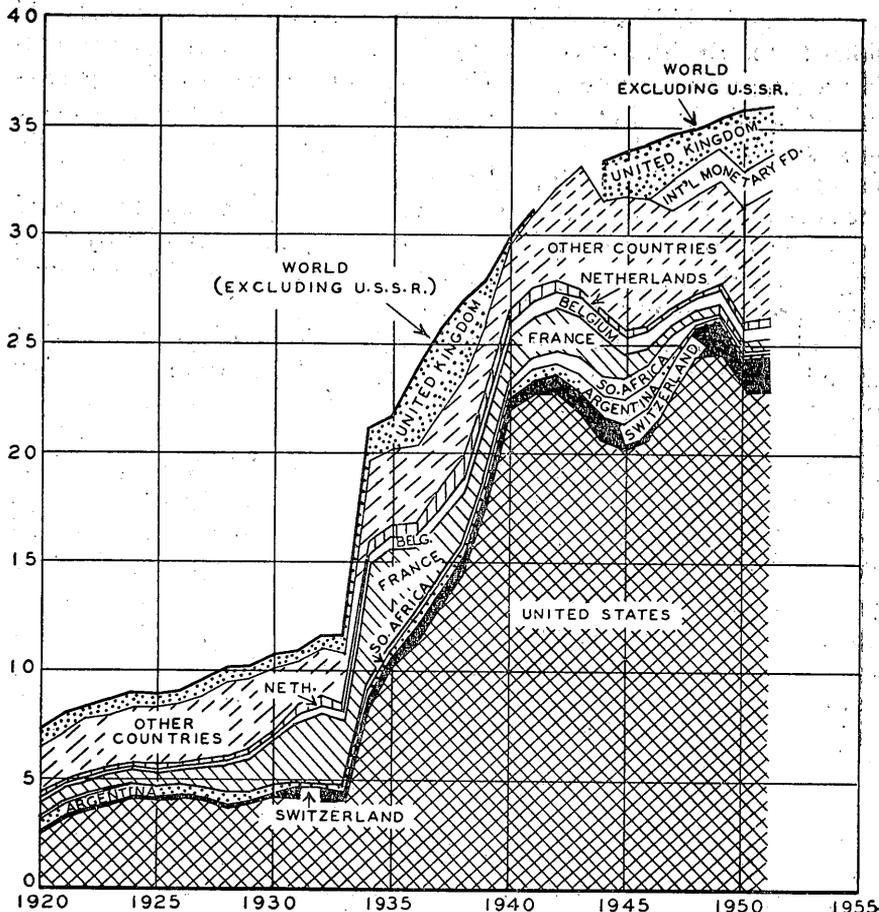
^b International Monetary Fund and Bank for International Settlements.

Note: Totals do not necessarily add up because of rounding.

WORLD MONETARY GOLD RESERVES:

(December 31; in billions of dollars at \$20.67 per fine ounce through 1933, thereafter at \$35)

BILLIONS OF DOLLARS



dollars that could eventually be "realized" by gold sales to the United States can best be appraised by comparison with the additions to international liquidity that the United States has made throughout the post-war years in the form of financial aid. The demand of the rest of the world for United States dollars during this period has been met by United States loans and grants. In the aggregate the United States Government thus extended, from July 1945 through December 1951, net foreign aid totaling 32.7 billion dollars, exclusive of United States contributions to the International Monetary Fund and International

Bank,¹⁴ or more than ten times the potential gold revaluation increment referred to above.

Of the hypothetical increment arising out of a gold appreciation, on the basis of the estimated gold stocks outstanding in December 1951, Great Britain, as banker of the sterling area, would receive, on the assumption of a price of \$44, roughly 565 million dollars, Continental Western Europe except Switzerland 750 million, Switzerland itself 370 million, Latin America 500 million, and Canada 220 million. The gold stock of the Soviet Union would also be given a higher dollar value. The greatest benefits would thus accrue to those countries already holding the most gold and not necessarily to those with the largest needs. Yet even these additions to monetary stocks, however considerable at first sight, would by no means be large enough to provide a basic remedy for the dollar shortage.

V. APPROPRIATENESS FOR THE UNITED STATES OF THE PRESENT DOLLAR PRICE OF GOLD

In dealing with the gold producers' case, it has already been pointed out that the present world price of gold can by no means be considered unrealistic in terms of the function of gold as a monetary metal; and in examining the international liquidity argument, it has been shown that raising the world gold price would not fundamentally remedy the world's dollar shortage, and accordingly the present price even from this angle cannot be regarded inappropriate. However, the considerations put forward thus far pertain essentially to countries other than the United States, whether gold producers or holders of gold stocks. It now remains to discuss the appropriateness of the world gold price from the viewpoint of the permanent economic interests of the United States itself.

Before undertaking a step as fundamental as that of raising the price of gold, the United States must consider whether it would not thereby inflict damage on itself—and indirectly on the world economy within which the United States occupies an important position. In effect, the United States gold policy cannot be divorced from domestic monetary and fiscal issues, the satisfactory handling of which bears directly upon the economic strength not only of the United States but also of the entire free world.

To start with, contentions sometimes heard in foreign countries that a rise in the dollar price of gold would be for the United States a pain-

¹⁴ See U.S. Department of Commerce, *Foreign Transactions of the U.S. Government* (Basic data through December 31, 1951), Washington, D.C., April 1952. For a comprehensive account of United States foreign aid, see *Survey of United States International Finance 1949, 1950, and 1951*, International Finance Section, Princeton University (published respectively in 1950, 1951, and 1952).

less way to extend financial aid can be disposed of quickly. Instead of raising the funds necessary for foreign aid through taxation, as has been done throughout the postwar years, the dollar price of gold might be increased; and by the same token the revaluation of the United States monetary stock would make possible an enlargement of the credit base of the banking system. The rise in the world gold price would thus, it is alleged, be beneficial to the United States itself. Yet, this counsel, however well intentioned, must be rejected as one of perpetual inflation; it could only work out as described if the United States did not take steps to eliminate the impact upon its own bank reserves, and even then the cost would be borne indirectly by American consumers through rising domestic prices. Under present-day conditions of full employment coupled with rearmament, neither the fiscal argument of alleviating the tax burden nor the monetary argument of providing a base for credit expansion can be used persuasively in support of a rise in the United States gold price.

A rise in the gold price, though reducing the monetary cost of foreign aid, would bring no relief to American taxpayers. Regardless of the form in which United States aid is given, its real cost to the American economy consists of the goods that are transferred from American to foreign consumption. What matters is therefore the size of the United States export surplus and the expansion in incomes to which it gives rise; whether this surplus is financed by gold imports or by United States Government foreign aid or in other ways is largely irrelevant so far as the impact on the American economy is concerned. Even if United States foreign aid appropriations were reduced under a higher dollar gold price, the problem of making goods available to foreign countries by reducing American domestic demand would remain. Instead of levying taxes to finance foreign aid, the United States Government would have to levy taxes to finance the gold inflow¹⁵—so long as it was determined to offset the inflationary pressures brought about by an export surplus. Therefore, even if the higher gold price made it possible to substitute increased gold purchases for a corresponding amount of foreign aid, the level of taxation would still have to be maintained at a figure high enough to

¹⁵ Normally, the United States Treasury pays for imported gold by drawing upon its balances with the Federal Reserve Banks; it may then replenish its funds by issuing equivalent amounts of gold certificates to the Reserve Banks. [As a matter of convenience, the Treasury issues gold certificate credits rather than printing and delivering gold certificates.] The process has an expansionary effect on the domestic credit situation unless the Treasury refrains from issuing gold certificates and replenishes its deposits instead from additional tax revenue or by borrowing from the public (borrowing from the commercial banks or from the Federal Reserve Banks would further expand the credit base), or unless the Federal Reserve System offsets the gold inflow by government security sales on the open market, or by raising reserve requirements if they are not yet at their legal maxima.

finance the increased gold inflow, since only in this way could the gold inflow be prevented from continuously expanding the money supply.

As to the monetary argument that the gold inflow would provide a base for further credit expansion, the answer is that the Federal Reserve System has had to operate throughout its life, with some brief intervals in the 'twenties and in the early 'thirties, against an avalanche of gold not responsive to ordinary methods of regulation.¹⁶ The Federal Reserve Banks have found it necessary at certain times to offset the gold imports by the sale of securities in the open market, and at other times by raising member bank reserve requirements.

Some foreign observers of United States monetary policy agree that the American banking system is in no need of further expanding its credit base. Nevertheless, they make an important reservation, namely that if and when deflationary pressure reasserts itself again in the American economy, the United States is likely to be less reluctant to raise the dollar price of gold. This reasoning, however, is also subject to grave doubts. Even under the hypothetical conditions of declining economic activity and growing unemployment it would not necessarily be in the national interest of the United States to raise the dollar price of gold merely to sustain an export surplus for the sake of domestic employment. Within the framework of the United States economy, the foreign demand is merely supplementary;¹⁷ and to whatever extent it might be deemed to need an increase, this could be achieved more effectively in the form of foreign aid, even if deficit-financed, than by raising the gold price. The domestic effect of these two forms of sustaining an export surplus would be the same in both cases; but even at a time of declining economic activity foreign aid would retain its advantages over gold appreciation inasmuch as it could be directed where it appeared to be most beneficial while the impact of a higher gold price would be entirely a matter of chance.

When in 1950 and early 1951, under the impact of a reversal in the various foreign balances of payments, gold flowed out in large amounts from the United States, some foreign commentators argued that the United States might be more inclined as a gold seller to raise the gold price than in its previous position as the world's greatest gold buyer. By maintaining the gold price unchanged, the United States was working against its own interests, it was alleged in some quarters, inasmuch as the readjustment of the price would add to the exchange value of gold

¹⁶ For a comprehensive account of the impact of gold inflow on monetary conditions and policy in the United States, see E. A. Goldenweiser, *American Monetary Policy* (McGraw-Hill Book Company Inc., New York, 1951), pages 177-178, 258-261, and 262-269.

¹⁷ United States merchandise exports have represented in recent years merely 4 to 6 per cent of the gross national product.

drawn from its monetary stock and thus reduce considerably the gold outflow.

These foreign views failed, however, to take into account the conditions under which the gold outflow actually took place. Prior to mid-1950, the improvements in the foreign balances of payments were made possible by increased output and by a subsidence of inflationary pressures in many countries, together with the 1949 currency readjustments and the reversal in speculative capital movements—a course of development to which the United States had itself considerably contributed by its postwar foreign aid. After the outbreak of Korean hostilities and the present international emergency, the sharp rise in raw material prices improved the balances of payments of raw-material countries—and as a result, Canada, Latin America, some Far Eastern countries, and also Great Britain, the banker of the sterling area, accumulated gold and dollar reserves. This redistribution of gold was generally regarded in the United States as being fundamentally in its own interest. Indeed, it was the declared United States policy that the countries receiving United States aid should not be required to reduce their reserves as a prerequisite of United States aid, although economic assistance on a grant basis was not to be extended for the purpose of increasing gold and dollar reserves.¹⁸ The basic objectives of United States foreign economic policy—namely the substantial relaxation of import and exchange controls, and especially the elimination of the discriminatory features of such controls, the restoration of general convertibility of currencies, and the promotion of multilateral trading—cannot be achieved without larger monetary reserves (gold and foreign exchange) for foreign countries.

Nor was there, under the conditions prevailing in 1950 and early 1951, any reason for the United States to consider raising the world gold price, under the International Monetary Fund's Articles of Agreement, for the sake of preventing the gold outflow from affecting the reserves of the Federal Reserve Banks. The statutory minimum reserve requirement is 25 per cent of combined note and deposit liabilities of the Federal Reserve Banks; when the gold stock was lowest in mid-July 1951, the ratio was 45.7 per cent, so a considerable margin of cover remained. After the reversal in the gold flow, with the subsequent increase in gold stock, the reserve ratio increased to 48.1 in mid-May 1952. Those foreign observers who are counting on a rise in the dollar price of gold if a loss of gold by the United States or an inflation of currency and credit should bring the ratio of gold stocks to Federal

¹⁸ National Advisory Council on International Monetary and Financial Problems, *Semiannual Report to the President and to the Congress, for the period October 1, 1950-March 31, 1951*, Washington, D.C., pages 9 and 10.

Reserve liabilities to near the legal minimum of 25 per cent will probably have to wait a long time.

Finally, and most decisive of all, the real strength of the United States dollar does not come from the monetary gold stocks but from the capacity of the United States to produce goods relatively cheaply and to supply them in very great quantities to the markets of the world. The United States can do so partly because it has large real resources and high productivity, and partly because inflation has been less in the United States than in most other countries. Furthermore, the insistent demand for improvement in living standards, economic development, and the requirements of defense are likely in other countries to exert inflationary pressures that, in terms of their relative resources and productivity, will very probably be much greater than comparable inflationary pressures in the United States. This basic strength of the United States dollar must not, however, give rise to any complacency; nor should we rely on a mere increase in output and productivity to safeguard the United States dollar. The fear lest a creeping inflation undermine the dollar cannot yet be dismissed. Nevertheless, as long as the American economy retains its vitality, flexibility, and adaptability and adequate anti-inflationary controls are resolutely implemented,¹⁹ the United States dollar is likely to retain its present international standing, and there is accordingly no ground whatever for increasing the dollar price of gold.

VI. THE FUNCTION OF A STABLE UNITED STATES DOLLAR PRICE OF GOLD IN THE WORLD ECONOMY

The gold policy of the United States rests on a fixed point of reference, namely the United States Treasury price of gold of \$35 per fine

¹⁹ For a discussion of the relationships between domestic conditions and policies in the United States and international gold movements, see "International Flow of Gold and Dollars, 1951," *Federal Reserve Bulletin*, March 1952, pages 227-236. This article notes in particular that "The most important immediate factor accounting for the cessation in the conversion of foreign dollar holdings into gold appears to have been a marked change in foreign expectations relating to inflationary prospects in the United States. The rise in the wholesale price level in the United States ceased early in 1951, and prices remained fairly stable during the remainder of the year. Among the factors bringing about this change were the introduction of wage and price controls late in January 1951; an unexpectedly high level of civilian output; a reduction in the rate of consumer purchases following the wave of scare buying in anticipation of shortages and rising prices; and some reduction in international tension. In addition, there was the adoption of monetary and debt-management policies designed to minimize further monetization of United States Government securities through Federal Reserve purchases. This action in particular assured foreign monetary authorities that the United States was determined to take adequate steps to maintain the stability of its currency, and thereby largely removed the main motive to maintain a greater than normal portion of their reserves in the form of gold."

ounce. It appears therefore appropriate to review here, in its essential aspects, the legal status of the United States price of gold. The present gold price was established by the Presidential proclamation of January 31, 1934, under the authority conferred on the United States President by the so-called Thomas Amendment,²⁰ as amended by the Gold Reserve Act of January 30, 1934.²¹ In accordance with this proclamation, the gold content of the dollar was reduced from 25.80 grains nine-tenths fine (or 23.22 fine grains, as fixed in 1837) to 15 5/21 grains of gold nine-tenths fine (or 13.71 + fine grains), thus changing the gold parity of the United States dollar from \$20.67 + to \$35.00 a fine ounce. This reduction in the gold parity of the dollar to 59.06 per cent of its former parity fixed the value of the dollar in the foreign exchange market at about the level to which it had depreciated in 1933. The President's power to devalue the dollar to 50 per cent or to revalue it up to 60 per cent of its former parity expired on June 30, 1943. Only an Act of Congress can now alter the gold parity of the dollar. While certain sections of the Gold Reserve Act of 1934 may lend themselves to an interpretation that would give the Secretary of the Treasury discretion, under certain conditions, to buy or sell gold at prices other than \$35 per fine ounce, no use of such discretionary authority has ever been made by him, and the authority has in effect been nullified by the obligations assumed by the United States as a member of the International Monetary Fund. Furthermore, under the Bretton Woods Agreements Act of July 31, 1945,²² neither the President nor any person or agency may propose to the International Monetary Fund any change in the par value of the United States dollar or approve any such change unless Congress by law authorizes such action.

Under the Gold Reserve Act of 1934 the United States Government took possession of all monetary gold in the country, including that held by the Federal Reserve Banks; it withdrew gold coins from circulation; it provided that no gold should be coined; it made it unlawful, except under certain conditions,²³ for banks and the general public to hold gold

²⁰ Sections 43 and 44 of Act of May 12, 1933 (48 Stat. 51).

²¹ Act of January 30, 1934 (48 Stat. 337).

²² Act of July 31, 1945 (59 Stat. 512).

²³ In accordance with the Gold Regulations issued pursuant to the Gold Reserve Act, persons in the United States may, under certain conditions, obtain licenses which authorize them to acquire and deal in gold for legitimate and customary professional or artistic uses. Provision is also made for limited acquisitions of gold for such purposes without a license and for the dealing in certain types of gold without a license. The export of any gold, other than fully fabricated gold (or monetary gold owned by foreign governments and central banks, as explained in the text above) is permitted only under a license on condition that the gold is to be exported for customary industrial, professional or artistic uses and not for use as, or in lieu of, money.

and gold certificates;²⁴ and it provided that no currency of the United States should be redeemable in gold.

International gold transactions of the United States are confined to foreign central banks and governments and international institutions. The Federal Reserve Bank of New York holds a license under which it imports and exports gold, and holds gold in custody, on behalf of its foreign and international correspondents. Foreign gold may be imported without limitation in amount for direct sale to the United States Treasury, provided that such gold has not been unlawfully exported from the United States since March 9, 1933, and that it is not gold that was looted during the last war, which the Secretary of the Treasury, in his Declaration on Gold Purchases of February 22, 1944, stated he would not buy. On the other hand, gold is sold, either for export or for earmark, to foreign governments and central banks and to international institutions for the settlement of international balances and other legitimate monetary purposes. It is in this way that the United States maintains an international gold bullion standard. These purchases and sales of monetary gold at \$35 (minus or plus a handling charge of 1/4 per cent) a fine ounce make the United States dollar fully convertible within the meaning of the Articles of Agreement of the International Monetary Fund.

When gold is imported for sale to the United States Treasury, the latter pays for it by drawing upon its balances with the Federal Reserve Banks, while replenishing its funds by issuing equivalent amounts of special gold certificates to the Reserve Banks. This process is essentially the same as when gold itself was held by the Federal Reserve Banks, the only difference being that the title to the gold is in the Treasury while the Reserve Banks hold claims on it in the form of gold certificates.

While maintaining a fixed gold price and an international gold bullion standard, the United States has acquired some 64 per cent of the world monetary gold stock excluding the USSR.²⁵ The significance of this

²⁴ Except for a small amount of gold certificates issued prior to 1934 that have not been turned in, some of which may have been lost, destroyed, or sent abroad, the only certificates now outstanding are held by the Federal Reserve Banks.

²⁵ From 1934 to the end of 1941 the United States acquired 13.5 billion dollars' worth of foreign-owned gold because the United States dollar was in extraordinary demand, partly as a result of a flight of capital from Europe in search of safety, and partly under the impact of the rearmament boom that led to an increase in European imports of American goods. During the war years 1942-1945, the United States lost 2.6 billion dollars' worth, as the bulk of United States exports was financed by lend-lease aid whereas the United States paid in cash for the bulk of its enlarged imports and heavy troop expenditures abroad. From the beginning of 1946 through September 1949, the United States acquired 5.4 billion dollars' worth from foreign countries despite large-scale United States Government grants and loans for relief or reconstruc-

proportion of United States monetary gold stock in terms of the world monetary stock can best be seen if United States holdings are related to the position of the United States in the world economy. In terms of raw material consumption and industrial production, the United States appears to account for over one half of the world economy, excluding the USSR. In terms of these proportions, the American gold holdings can hardly be viewed as unduly excessive. As already noted, however, some redistribution of monetary gold stocks is generally regarded in the United States as being fundamentally in the country's national interests.

The United States dollar price of gold of \$35 per ounce is in turn the basis on which the par values of most of the world's currencies are expressed under the Articles of Agreement of the International Monetary Fund.²⁶ The United States price of gold and the exchange parities of currencies established under the International Monetary Fund are thus closely connected. In a world of shifting gold and currency relationships, the United States gold price therefore serves as an anchor for the world's currencies.

It was toward the United States gold price that prices on the free gold markets were tending to move in mid-1950, prior to the outbreak of hostilities in Korea and the present international emergency. The experience of many countries in the latter part of 1949 and the first half of 1950 thus showed that when the value of national currencies seemed real and indisputable to the peoples concerned, free-market and official gold prices tended to converge and there arose a reasonable prospect for a stabilization of the currencies. As the spread between the free market and official gold prices narrowed, dealings in gold as a commodity ceased to interfere with its use as monetary metal; and the commodity aspect of gold was submerged in its monetary aspects. Thus, in this respect, too, the maintenance of a stable gold price in the United States appeared at this crucial moment as a fixed point of reference.

Still another aspect of United States gold policy contributing to international recovery and domestic stability is the basic principle that the proper place of gold in the world's monetary arrangements is in the monetary gold reserves of the governments and central banks. The concentration of gold in the monetary stocks has been the declared policy of the United States since 1934 and of the International Monetary Fund

tion abroad, and despite direct controls on dollar expenditures in foreign countries. From September 1949 to June 1951 foreign countries were able to recoup 2.8 billion dollars of the gold they had lost to the United States in the early postwar years. Beginning July 1951, however, the United States began again to acquire foreign gold (1.0 billion in the second half of 1951).

²⁶ In accordance with Article IV, Section 1 (a), the par value of the currency of each member is expressed in terms of gold as a common denominator or in terms of the United States dollar of the weight and fineness in effect on July 1, 1944.

since June 1947. One of the first policy acts of the Fund was to issue in 1947 a statement of its views as to the desirability of channeling gold to the maximum extent practicable into official monetary reserves.²⁷ As world economic conditions improved up to mid-1950, gold in actual fact did flow largely into official monetary reserves, as already noted; and although it leaked away after the outbreak of hostilities in Korea, and although the Fund, reiterating its gold policy, had to leave its practical application to its member countries,²⁸ the post-Korean setback should not be allowed to obscure the pre-Korean achievement. If a single lesson emerges from the Fund's experience with its gold policy, it is that the only way to reduce the premium gold prices and curtail the disappearance of gold into private hoards is for each of its member countries to follow economic, fiscal, and monetary policies that will give people confidence in their currency. It is only thus that the world can be made ready for a concentration of gold into official monetary reserves.

By maintaining its gold price, by buying and selling gold freely in transactions with foreign governments and central banks for legitimate monetary purposes, and by sustaining the basis on which the International Monetary Fund has been called upon to create and operate an international payments system, the United States has become the pivot of the international gold bullion standard as it exists today. In an unsettled world, there is an overwhelming need for such a reliable anchor, and in view of the position of the United States in the world economy, that anchor must be the United States dollar and the fixed price of fine gold in terms of United States dollars. To maintain a fixed gold price is a part of the United States' responsibility as the leading financial nation of the world, and its contribution to the restoration of monetary stability.

VII. CONCLUSIONS

From the viewpoint of both the United States and the world at large,

²⁷ At that time, as will be remembered, the initial par values of currencies had only recently been agreed upon and were not yet tested under postwar conditions; and monetary reserves outside the United States were declining rapidly. The payments difficulties that led to the Marshall Plan were already visible. It was in these circumstances that the Fund's statement helped to focus the attention of the member countries on the dangers of premium gold sales, which tended to reduce monetary reserves, since much of the gold so disposed of went into private hoards. Premium gold sales also directly or indirectly contributed to exchange transactions at depreciated rates.

²⁸ In September 1951, as will be recalled, the Fund reaffirmed its belief that gold should be concentrated in official reserves and not allowed to leak away into private hoards. However, the Fund found it impracticable to require all its member countries, in widely different situations, to apply uniform controls. Accordingly, while it urged the members to support the economic principles of its established gold policy, it left to its members, subject to the limitations imposed by the Articles of Agreement, the practical operating decisions to ensure that gold should be held to the maximum extent practicable in official reserves rather than go into private hoards.

the maintenance of the present dollar price of gold appears imperative for the following reasons:

1. There is nothing fundamentally "unrealistic" in the present official gold price of \$35 per fine ounce. It is at this fixed price that the bulk of international transactions is effected. It is only because the largest holder and the largest buyer of gold—the Treasury of the United States—freely buys and sells gold at a fixed price that there is a floor below which the world gold price cannot fall. It is therefore the maintenance of a stable gold price in a steady market for monetary gold, rather than momentary profits in erratic free markets, that would seem to be in the fundamental economic interest of those countries that are either producing gold or holding considerable monetary stocks.

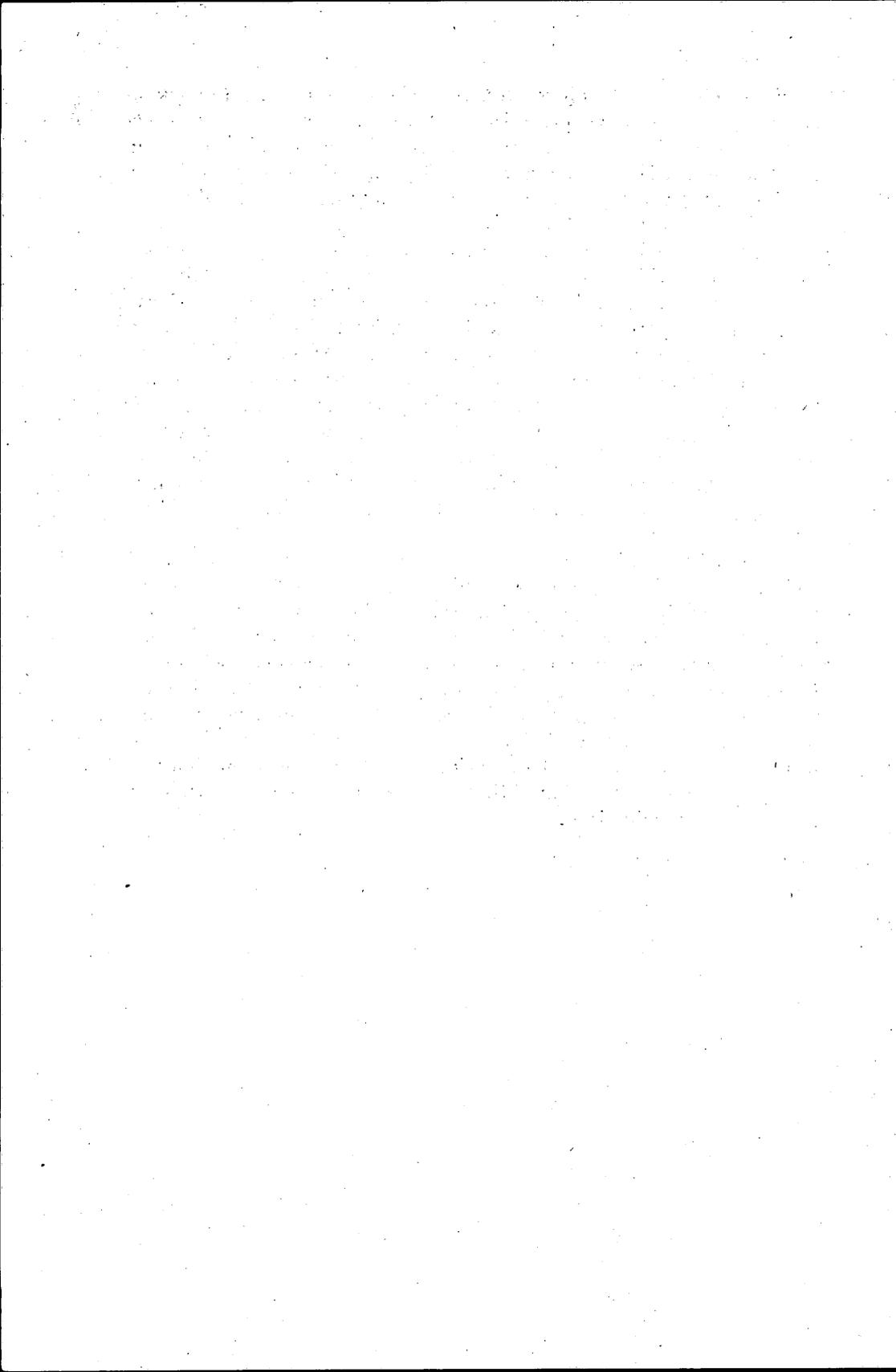
2. To argue that a rise in the commodity price level should be followed by an increase in the price of gold is a version of the economics of perpetual inflation. In the first place, the increase in the value of gold output, and gradually also in its volume, that would follow a gold price rise would increase the incomes in gold-producing countries, while there would be no parallel increase in the volume of consumer and investment goods; part of this added purchasing power would tend to spread itself into foreign countries through foreign trade and thereby increase the competition for goods. Secondly, increased sales of gold to monetary authorities by the producers would tend to expand the commercial banks' reserves and thus (unless offset, perhaps with some difficulty) increase their lending power. Thirdly, in the gold importing countries the reserve base of the banking system would also be enlarged. Finally, the psychological effect of a gold price rise would be decidedly inflationary. Under existing world-wide full employment coupled with rearmament efforts, a higher gold price would greatly complicate in many countries the task of monetary authorities in implementing policies of monetary restraint.

3. The potential gains for international liquidity and the foreign exchange reserves of other countries that might be derived from a gold price manipulation would be comparatively small, and their distribution uneven and haphazard. The addition to international liquidity would on the whole not be significant enough to bring lasting relief from the prevailing dollar shortage. Only those countries outside the United States that are holding large amounts of gold, and the large gold producing countries, would benefit materially; those with the greatest relative dollar needs would not necessarily do so. From a political point of view, too, an increase in the dollar price of gold would have the dubious effect of automatically increasing the value of the current output and the accumulated gold stock of the Soviet Union (apparently the second largest gold producer). Under present conditions the United States can make a more effective contribution to the alleviation of international pay-

ment difficulties by extending selective foreign aid rather than by taking in more gold at a higher price. In any event, the United States export surplus, financed to a considerable extent by financial aid to foreign countries, is already running at a rate about as high as is desirable. An increase in the world gold price would probably have to be fully offset by a reduction in United States foreign aid.

4. A world gold price rise is a deceptive formula and not a rational way of dealing with the political, economic, and social problems that the United States, the British Commonwealth of Nations, Continental Europe, and other parts of the free world are facing today. Furthermore, it may well be mistakenly regarded as a substitute for the effective measures, both domestic and international, that the Western nations will have to adopt to deal effectively with inflationary pressures and to meet their international payment difficulties. The fundamental task the world is facing is to promote economic growth, productivity and viability. The world would deceive itself in thinking that a gold price rise could, in some undefinable but automatic way, solve these fundamental problems for it.

5. The world needs a fixed point of reference for national currencies, and in view of the weight of the United States in world economy and finance, this point of reference today can only be the United States dollar and the dollar price of gold. This price, at which the United States is freely buying and selling gold in transactions with monetary authorities for monetary and other legitimate purposes, is the pivot of the international gold bullion standard and the basis of the new international payments system that the International Monetary Fund has been called upon to promote. The stability of this price is, in these uncertain times, of such great value to the United States as well as to the world at large that it must be maintained.



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