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# The IMF Gold Situation

On August 31 1975, the Interim Committee of the IMF (International Monetary Fund) released a communique on the proposed future role of gold in IMF arrangements. This proposal was adopted by the IMF Board of Governors at the Jamaica meeting in early January 1976. The communique states, in part, that, "... provisions should be made for ... sale of one sixth of *the Fund's gold* (25 million ounces) for the benefit of developing countries without resulting in a reduction of other resources for their benefit, and restitution of one sixth of *the Fund's gold* to members. The proportion of any *profits* or surplus value of the gold sold for the benefit of developing countries that would correspond to the share of quotas of the countries would be transferred directly to each developing country in proportion to its quota. The rest of *the Fund's gold* would be subject to provisions in an amendment of the Articles that would create enabling powers exercisable by an 85 percent majority of the total voting power."*

What is "the Fund's gold" that is being sold and restituted? What are the "profits" that will be made available to developing countries? The popular press has reported much about these IMF auctions, but we have found that these reports have left many questions unanswered. Herein we describe some aspects of the IMF arrangements in detail in an attempt to clarify the situation.

### *What Gold?*

When the IMF began operations in 1946, nations joining the organization were required to pay subscription fees equal in amount to their quotas, which were determined by the Fund. According to the IMF's Articles of Agreement, one purpose of these subscriptions was "to give confidence to members by making the Fund's resources available to them under adequate safeguards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity." In short, the IMF assets assured deficit members of available resources at times of need.

The subscriptions were paid in gold (valued at $35.00 per ounce) and in the currencies of the individual member nations. The minimum amount of gold required was the smaller of (a) 25 percent of the nation's quota to the IMF or (b) 10 percent of its official holdings of gold and U.S. dollars. (The U.S. dollar then was redeemable in gold by other countries.) Twenty-five percent of the United States' quota of $2.75 billion ($687.5 million) was paid in gold (19.64 million ounces).

On three occasions subsequent to the initial subscription, member nations made additional subscriptions equal to periodic increases in their quotas that were agreed upon. Each of these subscriptions was paid on the same terms as the initial subscription. Table 1 shows the total U.S. quota, or subscription, and the gold portion in the years of subscription payments. Note that the U.S. has paid approximately 47.9 million ounces of gold into the IMF as part of its subscription. The total value of that gold when it was paid was $1.675 billion (valued at $35.00 per cunce). However, at the current fiat-dollar price of gold (about $135.00 per ounce) that gold is worth about $6.5 billion.

Does the IMF now own that gold? Or, does it belong to the United States and is only held by the IMF? According to the Articles of Agreement of the IMF, if a nation withdraws from the Fund, the IMF is obligated to pay to it an amount equal to its quota plus any other amounts due from the Fund, less any amounts owed to the Fund. The Articles state, "Payments shall be made in the currency of the withdrawing member;" however, "if the Fund's holdings of the currency of the withdrawing member are not sufficient to pay the net amount due from the Fund, the balance shall be paid in gold, or in such other manner as may be agreed."

The Fund's holdings of the currencies of most of the major industrial countries are substantially less than its liabilities to those nations; therefore, if one of those members were to withdraw from the IMF, that nation probably would receive at least as much gold as it had contributed. However, a few major nations (such as Great Britain and Italy) and some of the developing countries, whose currencies the IMF holds in excess of the currency subscriptions, would not receive the gold originally contributed because of their debtor status. Therefore, a nation's claim on its gold subscription depends upon its status at the IMF. The United States is not an IMF-debtor nation, and it rightfully has a claim on all the gold that it has paid to the IMF. Thus, the gold being sold by the IMF is partly (about 23 percent) U.S. gold, not "The Fund's gold."

### *Gold Sales*

On June 2, 1976 the IMF auctioned 780,000 ounces of its holdings of gold. That was the first increment of gold sold by the Fund in accordance with plans to sell a total

Table 1
U.S. Quota in IMF
(Millions of units)

| Year | *Total Quota* | *$ Amount Of Gold* | *Ounces Of Gold* |
|---|---|---|---|
| 1946 | $2,750.0 | 687.5 | 19.64 |
| 1959 | 4,125.0 | 1,031.3 | 29.47 |
| 1966 | 5,160.0 | 1,290.0 | 36.86 |
| 1970 | 6,700.0 | 1,675.0 | 47.86 |

*Italicized words indicate our emphasis.

of 25 million ounces during a 4-year period. Although the stated purpose of these auctions is to provide financial assistance to the developing countries, the sales also are consistent with the asserted IMF attempt to "demonetize" gold, that is, to remove it from the official international monetary system. Because the "profit" from such sales is negligible in relation to the total debt of the less-developed countries, the sale of IMF-held gold to aid those countries seems to be a flimsy excuse. Of course, the monetary role of gold is not dependent on IMF sanction, but we shall not describe this matter here. (See *Research Reports* dated February 9, 1976 for such a description.) Here we shall discuss some possible effects of these auctions.

As Table 2 shows, the IMF has auctioned a total of approximately 3.9 million ounces of gold at 5 separate auctions. The average price paid for this gold has ranged from $109.40 per ounce to $137.00 per ounce. The total "profit" available to less-developed countries from the sales to date thus is about $320.6 million. "Profit" per ounce is the average price of the gold sold at each auction minus the dollar-equivalent of SDR 35.† Total "profit" is "profit" per ounce times the number of ounces sold at each auction. SDR 35 (currently about $40) is the value of an ounce of gold on the books of the IMF.

The 3.9 million ounces of gold sold thus far represent about 16 percent of the 25 million ounces that the IMF plans to auction. If the remaining gold were sold at the current market price of about $135 per ounce, a total of approximately $2.3 billion would be available to the developing countries. That sum is small compared with the estimated $50 *billion* that those nations owed to U.S. banks alone at the end of 1975. Obviously, the IMF gold auctions and Trust Fund arrangements can be of limited help to the developing nations.

Moreover, those nations as a group will receive only about 13 percent, their respective share of the quota, of the "profits" as direct payments. The remainder of the "profits" will be credited to a special Trust Fund from which eligible nations may borrow on concessionary terms for balance-of-payments needs. Such loans will be for 10 years and will carry an interest charge of only one-half of one percent per annum of the unpaid balance. Repayments will be made in 10 equal semiannual installments beginning in the sixth year of the loan. IMF provisions also state that a borrower will be able to request rescheduling of loan repayments, and the Trustee will be free to grant such rescheduling if it "finds that repayment on the date due would result in serious hardship for the member. . . ."

Following ratification of the Second Amendment to the Articles of Agreement by members (which IMF officials expect will be accomplished by late 1977), any nation eligible for assistance from the Trust Fund "will have an option . . . to submit noncompetitive bids" for "that part of the 25 million ounces that corresponds to the member's share in Fund quotas at the end of August 1975." (The text of this amendment was printed in *Research Reports* for February 2, 1976.) Such nations would have this option at one or more of the auctions, and users of the option would pay the average price per ounce paid by the successful bidders at that auction. Payment would have to be in currencies prescribed by the IMF, most probably the "strong" currencies only. If all eligible nations opted for gold, about 3.3 million ounces would be distributed by this procedure. However, this result does not seem probable. Most of the nations eligible to do this have severe balance-of-payments problems and insufficient amounts of "strong" currencies to purchase the gold. Only if they were permitted to use their own currency to pay for the gold could they simply print more such paper in order to obtain the ultimate reserve, gold.

†SDR is the abbreviation for Special Drawing Rights, originally defined as 1/35th of an ounce of gold, but now defined as the weighted average of 16 currencies.

Table 2
IMF Gold Auctions

| *Date* | *Sale Price per Ounce* | *Ounces Sold* | *"Profit" (millions)* |
|---|---|---|---|
| June 2, 1976 | $126.00 | 780,000 | $67.2 |
| July 14, 1976 | 122.05 | 780,000 | 63.9 |
| Sept. 15, 1976 | 109.40 | 780,000 | 53.8 |
| Oct. 27, 1976 | 117.71 | 779,200 | 60.3 |
| Dec. 8, 1976 | 137.00 | 780,000 | 75.4 |
| *Total* | | *3,889,200* | *$320.6* |

We should make one other comment about the gold sales. Although the IMF uses the word "profit" in describing the funds that will be available for developing countries, one should clearly understand that the funds in no sense represent "profit." The difference between the current market price of gold in fiat dollars and the dollar-equivalent of SDR 35 (the latter being the "price" of gold as valued by the IMF) simply reflects the depreciated gold-exchange value of fiat dollars. The distribution of phantom "profits" to eligible nations is a disguised form of foreign aid, and Americans are "contributing" about 23 cents of every dollar so distributed. This is an aspect of the situation not reported in the popular news media.

### *Restitution of Gold*

At the same time that the IMF Governors decided to sell one-sixth of the IMF's gold holdings, they also decided to return one-sixth of such gold to the nations that paid it to the IMF. This plan for restituting gold also is consistent with the announced intention of the IMF to eliminate the role of gold in the international monetary system. According to the IMF plan, gold will be restituted in proportion to each nation's quota. The U.S. quota is about 23 percent of the total IMF quota; therefore, this country will receive about 23 percent of the 25 million ounces to be restituted, or about 5.7 millon ounces of gold. The U.S. will pay the equivalent of SDR 35 (about $40) per ounce of gold, or a total of about $229 million. At the current market price of gold, that gold is worth about $774 million.

The plans for restituting the gold specify the return of the 25 million ounces in four equal annual installments. The first distribution is scheduled for January 1977.

The gold restitution plan also specifies that countries must pay for the gold in currencies acceptable to the IMF. Such currencies are those in demand at the IMF, currently the U.S. dollar, German mark, and Japanese yen. Those nations that have insufficient amounts of acceptable currencies, or those that decide not to use such reserves to buy the gold, will be able to postpone their acquisition of gold until the Second Amendment to the Articles of Agreement is ratified. Thereafter, those nations will be able to purchase the restituted gold with their own currency.

There has been much speculation about what the nations will do with the restituted gold. We can think of 3 possibilities: (1) a nation might hold the gold as part of its monetary reserves; (2) a nation might sell the gold on the open market for needed currency; or (3) a nation might use the gold as collateral for loans, as Portugal and Italy have done recently. In assessing what the nations might do with the gold, we have divided the member nations into 4 groups: (1) the United States, (2) other industrial countries, (3) oil-producing countries, and (4) less-developed countries.

As we reported above, the United States will receive about 8 million ounces of gold, which is by far the largest amount to be returned to any one nation. The U.S. Treasury currently holds about 275 million ounces of gold. An additional 8 million ounces thus will be an insignificant increase in the Treasury's holdings. Therefore, we believe that the policy of the United States regarding gold will be unchanged by the newly-acquired gold. The two U.S. Treasury auctions during 1975 totaled only 1.2 million ounces, and there have been no indications that Treasury officials have planned more gold sales. Of course, the United States has no need as yet to use gold as collateral for a loan, inasmuch as the fiat dollar remains the primary international currency. Therefore, we conjecture that the United States probably will hold in its reserves the restituted gold.

The other industrial countries, with the possible exception of Great Britain and Italy, also probably will retain their gold in their reserves. Officials of some European nations, including particularly those in France, have demonstrated an awareness of the usefulness of gold, and they probably will not sell it. Other nations simply do not need to borrow; therefore, they do not need it for loan collateral. Japan also has no need for loan collateral, and because that country owns only a small amount of gold, officials there probably will retain this gold in the monetary reserves. Italy and Great Britain probably will use the gold for balance-of-payments purposes. Italy already has gold-backed loan liabilities, and officials there probably would increase such borrowing rather than sell the gold outright. Italian officials have been reluctant to part with gold, but officials in Great Britain generally have viewed gold as a "barbarous relic." Therefore, we should not be surprised if they were to sell the gold returned by the IMF and to use the proceeds to reduce outstanding sterling liabilities.

The major oil-producing nations have balance-of-payments surpluses or relatively small deficits; therefore, they have no pressing need to use the gold as collateral or to sell it for currency. Moreover, all of these countries currently hold only minute amounts of gold as monetary reserves; thus, their officials might rejoice at the chance of obtaining gold so inexpensively. Indeed, recently we have read assertions that the central banks of some Mideast nations have acquired gold during recent months. We conclude that most of the gold restituted to the oil-producing nations will be added to monetary reserves.

Most of the less-developed countries have severe balance-of-payments deficits, and they probably will use their gold to help alleviate them. Whether they will sell the gold or use it as collateral, we should not guess. In either case, the impact on the gold situation will be minimal. Of the 25 million ounces of gold being restituted during the 4-year period, the 29 industrial countries and oil-producing countries will receive about 72 percent, or about 18 million ounces. The remaining 7 million ounces will be divided among 99 countries. The largest amount returned to a less-developed country will be approximately 800,000 ounces, which will be received by India.

### *The Remaining Gold*

The IMF is selling and restituting a total of about 50 million ounces of gold, or one-third of the gold in its possession. Inasmuch as the intention of the IMF is to remove gold from the international monetary system, what might the Fund do with the remaining 100 million ounces of gold?

Paragraph 7 (b) of the communique issued on January 8, 1976 by the Interim Committee of the Board of Governors states the Fund's position regarding this gold:

"The amended Articles would contain an enabling provision under which the Fund would be able to sell any part of the gold left after the distribution of 50 million ounces in accordance with the arrangements referred to in paragraph 3 above, and use the profits (1) to augment the general resources of the Fund for immediate use in its ordinary operations and transactions, or (2) to make balance of payments assistance available on special terms to developing members in difficult circumstances. On the occasion of such sales the Fund would have the power to distribute to developing members a portion of the profits on the basis of their quotas or to make a similar distribution by the direct sale of gold to them at the present official price. Any decision on such a distribution should be taken by an 85 percent majority of the total voting power. These powers of the Fund would be in addition to the power that the Fund would have under another enabling provision to restitute to all members, on the basis of present quotas and at the present official price, any part of the gold left after the disposition of the 50 million ounces referred to above."

When the Second Amendment to the Articles of Agreement is ratified the mechanism will be in place to either sell the remaining 100 million ounces of gold or to return it to the member nations in proportion to their quotas. Any action in either case would need approval by 85 percent of the total voting power. Because the United States will have about 21.5 percent of the voting power after ratification of this amendment, U.S. officials will have veto power over any IMF plans for distributing the gold. Thus far the position of U.S. officials with reference to gold has been similar to that of the IMF; therefore, we conclude that the IMF probably will distribute in some manner the 100 million ounces of gold remaining in its possession.

That this would signal an end to a monetary role for gold is most improbable. To the contrary, we should expect the monetary role of gold to increase as depreciating paper currencies and the SDR assume more prominent positions in the IMF. Perhaps the removal of gold from its assets will hasten the final demise of the IMF, a result that would aid the restoration of a sound international monetary system.

## DEMAND

### *RETAIL SALES*

Estimates of retail sales during the most recent week and 4 weeks compare with such sales during the corresponding periods a year earlier as follows:

| *Period* | *Percent change* |
|---|---|
| Week ended December 10 | +10 |
| Four weeks ended December 10 | +10 |

## BUSINESS

### *STEEL PRODUCTION, USES, AND PRICES*

During the first 11 months of 1976, domestic steel manufacturers produced 99.2 million tons of "raw" steel (ingots, castings and other first-stage forms of steel). This amount was 10 percent more than that produced during the corresponding period of 1975 but 14 percent less than the record amount produced during the first 11 months of 1973.

"Raw" steel production increased markedly during the first 6 months of 1976, but it has decreased markedly since June. Estimated "raw" steel production during November was 9.5 million tons, which was the smallest volume during any month this year.

According to reports, industry analysts currently expect that shipments of steel mill products by domestic mills will total about 90 million tons during 1976. This amount would be about 13 percent more than the 80 million tons shipped during 1975 but roughly 18 percent less than the amounts shipped during 1973 and 1974. The current estimate of 90 million tons is about 5 million tons less than industry analysts had predicted earlier in the year. One reason for the disappointing volume of shipments apparently was smaller-than-anticipated orders for steel mill products from "capital goods" manufacturers. The output of such manufacturers has been less than widely expected because total outlays for plant and equipment by U.S. businesses have not as yet increased substantially during the current business-cycle expansion.

Steel imports during 1976 are expected to total about 14 million tons, or about 2 million tons more than total imports during 1975. However, 1976 import volume would be less than imports during the years 1972 through 1974, when an average of about 17 million tons of steel mill products per year were imported. Exports of steel mill products by U.S. producers are expected to total about 2.6 million tons, which would be about 12 percent less than that last year and the smallest volume since 1968.

Executives of several steel manufacturing firms recently have charged that steel production for export is being subsidized abroad, and they have suggested that "countervailing duties" should be imposed by the United States. Such charges are not new. That they have been made again at this time apparently reflects the disappointing demand in the domestic market rather than any unusual increase in imports. The estimate of 14 million tons of imports during 1976 approximates the volume widely forecast earlier this year.

The index of iron and steel prices during November was 7.3 percent more than that a year earlier; however, most of this increase occurred during the first half of the year. The level of the index for November was slightly less than the record level reported for July. Last summer steel producers announced price increases on some products to be effective on October 1; however, the increases were rescinded before they became effective. At the time of rescission, mill spokesmen stated that "market conditions" would not support the price increase. The long advance notice given to customers then may have contributed to the uneven pattern of steel production during 1976, as steel users apparently increased their inventories during the summer in order to reduce the impact of the announced higher prices. Mill orders decreased markedly after September, as steel users purchased less steel than they used.

During the Thanksgiving holiday weekend, steel producers announced a 6-percent price increase, effective December 1, on flat-rolled products, which comprise 40 or more percent of total shipments. Flat-rolled steel is used by automobile and appliance manufacturers and by can makers, among others. That customers received brief advanced notice of this increase gave them little opportunity to increase purchases before the effective date. Inasmuch as "market conditions" appeared to have improved little since September, the price increase surprised many analysts. However, the official prices probably do not reflect transaction prices, given the countless opportunities available to offer customers more favorable delivery, credit, or quality terms. One large purchaser stated, "It will take the steel companies two or three months to push their realized prices up to the new and higher level, even assuming the demand does improve a lot." One reason for the timing of the price increase might be that the producers wanted to avoid a direct confrontation with the Carter administration about steel prices for as long as possible.

The composite price of No. 1 heavy melting scrap, as reported in *Iron Age*, averaged $64.30 per long ton during November. This average was 10 percent more than that a year earlier, but 30 percent less than that during April, when the monthly average price was the highest of any of the first 11 months of 1976. The marked decrease of the price of steel scrap since April reflects decreased demand from the mills. The trend of weekly steel scrap prices has been upward since October 25, when the price was $62.83. On December 6, steel scrap was priced at $66.50. The recent increases might indicate that an end to the downward trend of steel production is imminent. Indeed, recent steel production data suggest likewise.

***There are some signs that the downward trend of steel production might have ended. However, steel production probably will not be large until total plant and equipment expenditures of U.S. businesses increase substantially.***

## SUPPLY

### *INDUSTRIAL PRODUCTION*

Production of steel, automobiles, and electric power (1) in the 1- and 4-week periods ended on the indicated dates in the current year and (2) in the corresponding periods of earlier years was as follows:

| *Steel* | *1929* | *1932* | *1973* | *1974* | *1975* | *1976* |
|---|---|---|---|---|---|---|
| Ingots (million tons) | | | | | | |
| 1 week: December 11 | 0.88 | 0.23 | 2.93 | 2.49 | 2.10 | 2.14 |
| 4 weeks: December 11 | 3.74 | 1.03 | 11.76 | 10.12 | 8.26 | 8.52 |
| *Automobiles* | | | | | | |
| Vehicles (thousands) | | | | | | |
| 1 week: December 11 | 24 | 18 | 189 | 130 | 171 | 208p |
| 4 weeks: December 11 | 95 | 45 | 766 | 468 | 605 | 717p |
| *Electric Power* | | | | | | |
| Kilowatt-hours (billions) | | | | | | |
| 1 week: December 11 | 1.8 | 1.5 | 34.7 | 37.1 | 38.2 | 42.6 |
| 4 weeks: December 11 | 7.2 | 6.0 | 137.7 | 143.5 | 147.9 | 163.5 |

Percent change from 4 weeks a year earlier: +10.5

p Preliminary.

## PRICES

### *PRICE OF GOLD*

| | *1975* | *1976* | |
|---|---|---|---|
| | *Dec. 18* | *Dec. 9* | *Dec. 16* |
| Final fixing in London | $138.90 | $136.50 | $134.40 |

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