

The Economic Club of New York

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The Honorable Dean Rusk  
Secretary of State

And

The Honorable Alfred Hayes  
President, Federal Reserve Bank  
of New York

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The Stake in Vietnam

There are many subjects which I would be tempted to discuss this evening. Many would be the basis for encouragement and confidence, for the Free World is getting on with its job. Others would cause concern and anxiety because they remain difficult and dangerous. I hope you will let me address myself to one of the latter this evening – a seemingly remote sector of the great worldwide struggle between freedom and coercion, a sector often poorly understood if not deliberately misrepresented, but a sector of vital importance to the future health and security of the Free World. I refer to Vietnam.

Vietnam is a narrow strip along the South China Sea, nearly as large as California, with a population of some 30,000,000 – about 16,000,000 in the north, and about 14,000,000 in the south.

With Cambodia and Laos, Vietnam formed what was formerly known as French Indo-China. During the Second World War, the Vichy regime yielded control of French Indo-China to the Japanese. In the spring of 1945, the Japanese proclaimed the independence of Vietnam. And in August of that year they permitted the Communist-oriented Viet Minh to seize rule. In the Indian

subcontinent, Burma and the Philippines, western countries recognized at war's end that national demands for independence would have to be met promptly. This was not so with Indo-China. The returning French met, therefore, a militant resistance movement. For eight years, with material help from the United States, they sought to pacify the country.

Nominally, the leader of South Vietnam was the Emperor Bao Dai, absent much of the time from his country. The Prime Minister was a Vietnamese nationalist, Ngo Dinh Diem. He was not well known at the time to most of his own countrymen, at least compared with a name like Ho Chi Minh. He had to build a government and create a national administration out of almost nothing. And he was surrounded by enemies. The Communists hated him. So did many of the local French, who had not yet become reconciled to a genuinely independent Republic of Vietnam. So did some of the South Vietnamese politicians. Rejecting both Communists and collaborators with the former colonial regime, his political base was narrow and able assistants were not easy to find.

Very few observers either in the West or in Asia gave either Prime Minister Diem or the Republic of South Vietnam much chance of survival. Many expected the Communists to take over within a few months.

Into this chaos poured nearly one million refugees from North Vietnam. Many were diseased, many suffering from starvation; some bore scars from Communist torture. They brought nothing

but the clothes – or rags – on their backs and the will to work and live in freedom. These were the intrepid people of whom Dr. Tom Dooley wrote so movingly in “Deliver Us From Evil” – who led him to devote the rest of his all too short life to helping the people of Vietnam and Laos. In that book Dr. Dooley said of the people of Vietnam: “Americans never fail to like the Vietnamese when they get to know them. It is impossible not to respect their driving compulsion for freedom...”

Despite the long odds against success, President Eisenhower and Secretary of State Dulles wisely resolved to assist South Vietnam. The United States provided economic assistance, a military training mission and weapons.

What happened in South Vietnam during the next five years deserves to be listed near the top of the success stories of the post-war period. By plebiscite, the Emperor Bao Dai was replaced by a Republic, with Ngo Dinh Diem as President, an elected National Assembly, and a written Constitution. The independent armies of the religious sects were dissolved. The nearly 1,000,000 refugees from the North were resettled and resumed earning their own living. A land reform program, patterned on the land reforms in Japan and on Taiwan, was pressed forward – 123,000 heads of families became small land owners. A comprehensive system of agricultural credit was set up. Thousands of Vietnamese were moved into the highlands to raise industrial crops. Rubber production rose and new plantings of better varieties promised still higher production for the future. Sugar production doubled in 1958. South Vietnam was soon producing enough rice to

resume exports on a rising scale. Various small industries were established. Textile production rose from near zero to near self-sufficiency. Electric power nearly doubled. Per capita national income rose by 20 percent.

Thousands of new schools were built. Between 1956 and 1960, enrollment in the elementary schools rose from 400,000 to 1,500,000. The expansion of health facilities included new hospitals and 3,500 village health stations. Rail transportation was restored. Roads were repaired and improved, and three new major highways built.

The Communists were not completely eliminated – especially along the land and sea frontiers, where they could be supplied – but most of South Vietnam became safe for travel.

Although North Vietnam inherited most of the industry of Vietnam, and although its population is larger, it fell rapidly behind South Vietnam in food production, number of children in school, and standards of living. While per capita food production rose 20 percent in the South, it fell 10 percent in the North.

This was competition which the Communists apparently could not endure. Very likely it was one of the reasons why they declined in 1959 to renew their assault on South Vietnam. And in 1960 the Lao Dong Party – that is the Communist party – ordered the “liberation” of South Vietnam.

According to Communist propaganda, the war in South Vietnam is a civil war, a local uprising. The truth is that it is an aggression organized, directed, and partly supplied from North Vietnam. It is conducted by hardened Communist political organizers and guerilla leaders trained in North Vietnam, who, upon their arrival in the South, recruit local assistance. This has been done in a variety of ways, including terror and assassination. School teachers, health workers, malaria eradication teams, local officials loyal to the Republic – these were the first targets of the assassins. But many ordinary villagers who refused to cooperate with the Communist guerillas likewise have been ruthlessly killed.

This assault on South Vietnam was a major Communist enterprise, carefully and elaborately prepared, heavily staffed, and relentlessly pursued. It made headway. In 1961 President Diem appealed for further assistance and President Kennedy responded affirmatively.

The strategic importance of South Vietnam is plain. It controls the mouth of the Mekong River, the main artery of Southeast Asia. The loss of South Vietnam would put the remaining states of Southeast Asia in mortal danger.

There are larger reasons why the defense of South Vietnam is vital to us and to the whole Free World. We cannot be indifferent to the fate of fourteen million people who have fought hard against communism – including nearly one million who fled their former homes to avoid living under Communist tyranny. Since we went to the aid of Greece and Turkey 16 years ago, it has

been the attitude of the United States to assist people who resist Communist aggression. We have seen this form of attack fail in Burma, Malaya, and the Philippines. The South Vietnamese are determined to win their battle and deserve our help.

Critics have complained that South Vietnam is not a full constitutional democracy and that our aid has been subject to waste and mismanagement. In passing judgment, let us recall that we are talking about a nation which has been responsible for its own affairs for less than a decade, about a people who have had no peace since 1941 and little experience in direct participation in political affairs. Their four national elections, their thousands of elected hamlet councils, and their forthcoming village council elections show steady movement toward a constitutional system resting upon popular consent.

Let us also recall that Vietnam is fighting a war – a mean, frustrating and nerve-wracking struggle – and fighting it with courage and determination. The overriding unfinished business is to achieve public safety in order that the country can resume its march toward peace and prosperity. This in itself requires the utmost effort in good administration, in the effective use of available resources, as well as dedicated leadership of an aroused people. I do not defend mistakes or failures which can be put right; but I do wish to enlist your understanding for an effort which includes perseverance, gallantry, and sacrifice. I have no doubt about the ability of South Vietnam to take an honored place among modern nations as it rids itself of the enemies gnawing at its vitals.

Our role in South Vietnam is a limited and supporting role. We provide technical, logistical, training, and advisory assistance. We have no combat units as such in South Vietnam, although many of our military personnel – and some civilians – come under fire in combat situations and we have suffered some casualties. The some 12,000 men we have there are among our finest; their skill, courage, and dedication make debtors of us all.

I would point out that we are not alone in assisting the Republic of Vietnam. Ten other nations are helping in one way or another. We hope that they will do more and that many other non-Communists will contribute. For the whole Free World has a vital interest in the defeat of this Communist aggression against South Vietnam.

Understandably, there are occasional differences of view between the government in Saigon or Vietnamese officers in the field and their American advisers. But they and we are all committed to success for the Republic of Vietnam. It is the Vietnamese who are waging the war. Some 4,000 Vietnamese soldiers were killed and some 6,000 wounded in action during the past year. They exacted nearly 30,000 casualties in return.

Colonel Serong, Commander of the Australian Advisers in Vietnam, has said: “The typical Vietnamese soldier is as good as you will find. He is brave and he is tough.” We believe that the Vietnamese, with our help, have developed winning tactics. With the assistance of helicopters, airplanes, and radios the government forces are able to maintain the initiative and, increasingly,

to achieve the advantage of surprise.

The strategic hamlet program is producing excellent results. A strategic hamlet is a hamlet with a defensive perimeter and a trained and armed militia. Usually it also has a radio with which to call for help if it is attacked.

As the Communist attack is political and economic as well as military, so is the response. The government of Vietnam – and we – attach the greatest importance to the civic action side of the strategic hamlet program. The hamlets are governed by councils elected by secret ballot. In addition – and not least important – the government is supplying the hamlets with schools, medical aid, cheap fertilizer from government-supported cooperatives, low interest agricultural loans, and other agricultural extension services.

Already approximately 7,000 Vietnamese live in well over 5,000 strategic hamlets. The program calls for the completion of another 3,000 by the end of this year. Morale in the countryside has begun to rise. An estimated half a million people formerly under Viet Cong control now have increasingly effective government protection.

The strategic hamlet system provides strength against the Communists in the countryside. The Communists are no longer, in Mao's figure of speech, fish swimming in a sea of peasants. Every bush is no longer their ally. They are getting hungrier. To the Vietnamese peasant they look less

and less like winners.

The villagers are fighting when attacked, and are volunteering all important information to the government forces. Thousands of the Montagnards – the hardy mountain tribesmen – have been armed and trained to fight.

Rice production is up and rice exports have been resumed. Defections from the Viet Cong have risen – though these are mostly locally recruited auxiliaries, not the hardened Communist cadres. The Viet Cong is losing more weapons than are the government forces. Viet Cong attacks are running at less than half the rate of January, 1962. Several Viet Cong strongholds have been penetrated and supplies and installations destroyed. The Viet Cong has been unable to carry out its plan to escalate to larger military units and more conventional warfare.

The Communists have a lot at stake in this struggle and will not quit easily. But the men and women who were deceived and exploited, or enrolled by force, by the Communists now have a chance to rally to the side of the national government. Last week, on the first anniversary of the initiation of the strategic hamlet program, President Diem proclaimed Campaign Open Arms. This is an offer of clemency and assistance and jobs to all who desert the Communists. Even those who have trespassed against the law, and have already been condemned or who are subject to court trial, may redeem themselves by “meritorious patriotic acts.”

We applaud this statesmanlike offer. It is similar to the one the late great Ramon Magsaysay used with such good effect in breaking the power of the HUKS in the Philippines a decade ago.

Communist aggression against South Vietnam is, of course intimately related to the refusal of the Communists to give full support to the Geneva Accords on Laos. Although it was not my intention to speak of Laos this evening, the most recent events in that unhappy land-locked country call for brief comment. The Pathet Lao, with strong backing from Hanoi and other Communist countries, have refused to give Prince Souvanna Phouma and his coalition the support and cooperation which were pledged at Geneva. The international machinery established by those Accords has not been allowed to function with full effect. The writ of the Central Government has not run in Pathet Lao controlled areas. Viet Minh military personnel have not been fully withdrawn.

We are making every effort to ascertain whether all signatories of the Geneva Accords are prepared to support those agreements or whether some are moving to destroy them. If those agreements collapse, most serious and dangerous issues will arise and once again we shall have to determine what steps can be taken to insure that the Laotian people are left alone in peace and not be overrun and exploited by those who would commit aggression.

Returning to Vietnam: We cannot promise, or expect, a quick victory there. The enemy is elusive and determined; and relatively small numbers can disrupt the normal processes of a going

society. It took eight years to wipe out the Communist terrorists in Malaya – and they were far from a major Communist base.

But there is a good basis for encouragement. The Vietnamese are on their way to success and need our help; not just our material help but our sympathetic understanding and comradeship. I can understand the discontent which surrounds any important task still unfinished. I cannot understand anyone who would quit, withhold our resources, abandon a brave people to those who are out to bury us and every other free and independent nation. That we cannot and will not do.

The Honorable Alfred Hayes

President, Federal Reserve Bank of New York

The Dollar: National and International Bulwark

I should like to talk to you tonight about the dollar--the role it plays in the world and the urgent problems we face if we want to see that role maintained. My theme runs about like this: The strength of the United States, both at home and abroad, is inextricable linked with the strength of the dollar, and the dollar, in turn, is a key component of the Free World's financial structure.

While the dollar still commands a high degree of confidence, there has been a perceptible lessening in its relative strength during the past five years of heavy international payments deficits for the United States. Despite all our efforts to date, and some of them have been quite effective, the payments deficit remains much too high. A prolongation of heavy deficits cannot fail to damage the dollar badly, and to damage along with it the payments system that has fostered economic growth here and abroad since the end of World War II. As a nation, we have the power to arrest and reverse these deficits, and to do so in a way that will preserve the basic structure that we want. Like all major national issues, the problem is one of priorities, in this case, whether we are willing to assign a top priority to the goal of restoring the dollar's unquestioned standing.

The dollar attained pre-eminence in much the same undirected, almost unconscious, way that the

United States became a great nation. Gradually, it became the medium of exchange for a large part of the world's trade and investment transactions, sharing this role principally with the pound sterling. Beyond this, the special role of the dollar as a standard and store of value was clearly recognized in the Bretton Woods Agreement of 1944, which provided for world currencies to be valued in either gold or the dollar. Indeed, the world's monetary reserves now consist largely of gold and dollars.

The role of the dollar as a reserve currency rests on several considerations: (1) a strong United States economy, in which the dollar is expected to remain immediately usable for a wide variety of goods and services at reasonable stable prices; (2) a strong United States creditor position in the world, with our foreign assets, largely long-term, exceeding our total foreign liabilities by a substantial margin; (3) our large gold stock, now comprising some 40% of the world's monetary gold, and available to foreign monetary authorities at the fixed price of \$35.00 per ounce.

Faith in a currency has the quality of being scarcely noticeable until there is a reason to question it. Until recently, the dollar's impregnable position was so taken for granted that few observers bothered to analyze carefully what lay behind this strength and what might endanger it. We can all recall the concern for those nations in Europe and elsewhere that faced a so-called permanent dollar gap". Yet, within a few years, the dollar has lost some of its luster and is no longer immune from occasional fears and suspicions. At home, the conclusion is inescapable that concern over the dollar's future is, in Chairman Martin's words, "a major shadow over our

economy”; restraining that full flowering of business confidence that is essential to the vigorous economic growth we all seek. The question naturally arises whether we should welcome or deplore the unique position of the dollar, in short, whether the burdens of a key currency are worth bearing. This is not the place for lengthy analysis, but I believe the tangible and intangible benefits from this rose are great. Clearly we must recognize the importance of a strong dollar if our national voice is to carry full weight in political, military, and economic dealings with other nations. It is clear too, that only a dollar of unquestioned soundness can continue to share with gold the role of providing the world’s monetary base. Moreover, I cannot conceive how we could relinquish the key position of the dollar, even if we were will to, without also isolating ourselves from our partners in world trade and payments, obviously at enormous real cost.

Even if our international payments were now in balance we would still have the responsibility, as the world’s leading banker, for running our internal affairs so as to maintain the confidence of our foreign depositors and our own people. For those foreign dollar holdings, representing an accumulation of past deficits, confront us with a sobering relationship between our liquid assets and liabilities. But the position of the dollar would be far stronger if we put a stop to the deficits that have reduced our gold stock and swelled our short-term indebtedness to the rest of the world.

Before considering ways to eliminate the balance-of-payments deficit, let’s recall how it has been financed to date. Over the past five years the deficits have aggregated about 16 billion

dollars. Of this, 7 billion dollars was paid for through sales of our monetary gold. Another 7 billion dollars was financed through increases in dollar holdings of official foreign and international monetary authorities, while the private dollar holdings of foreign banks, corporations and individuals increased about 2 billion dollars. There are limits, however, to the willingness of either official or private foreign entities to add to their holdings of dollars. Relatively easy credit conditions in this country tend to discourage private holders of dollars, even though the Federal Reserve System and the Treasury have sought to prevent this easy credit from being translated into excessively low short-term interest rates. To the extent that dollar investments appear unattractive to these private holders as compared with investments in their own or other countries, the dollars tend to find their way into foreign central banks' reserves. Once these official dollar holdings reach ample levels, there is naturally a reluctance in some countries to further enlarge the dollar component of their growing monetary reserves, and they tend to use additional dollars to buy gold.

Until a year or two ago these gold outflows or increased dollar holdings were the only means for settling our deficits with foreigners. But in recent months the Federal Reserve has arranged reciprocal currency drawing rights with most of the countries of major importance in international payments, while the Treasury has also acquired foreign exchange by issuing United States bonds denominated in foreign currencies. These arrangements, eliminating any exchange risks, have been useful in reducing immediate claims on our gold, and in avoiding or moderating temporary imbalances such as those caused by international tensions or speculative pressures

against other currencies as well as the dollar. The stability of the exchange markets during the Cuban crisis was a good case in point. These Federal Reserve and Treasury arrangements mark new milestones along the path of more effective international financial cooperation, which I am happy to say has not been affected by the recent policy differences among the major western nations on the military and trade fronts.

There are also other major means of financing a deficit, at least temporarily, which are still untapped and which constitute a most important reserve. I am thinking specifically of the normal resources as well as the enlarged lending facilities of the International Monetary Fund. But so long as the United States is in the process of correcting a long-continued deficit, the Fund is probably best regarded as pretty much a “lender of last resort”; it would be foolhardy to neglect going to the root of the problem because of the existence of these special resources. And besides, it is obvious that any borrowing from the IMF is only a respite and that future repayment of such borrowing would require not merely equilibrium in the balances of payments but actual surpluses.

I have heard our swaps and foreign currency borrowings criticized as “cover ups” that cause us to lose sight of the underlying need for payments equilibrium; but I can assure you that neither the Treasury nor the Federal Reserve has had the slightest illusion that they are in any sense a substitute for the needed remedial actions. Rather, apart from their longer-term value as a

contribution to world liquidity, they serve at present as a holding operation while we undertake, by more fundamental measures, to get our basic payments deficit under control.

This brings us to the nature of the deficit itself. The bare bones of this problem can be set out as follows: (1) we have heavy government commitments abroad, military and economic; (2) we have large private capital outflows, including direct investment, long-term portfolio investment and volatile short-term flows; and (3) while we sell more goods and services abroad than we buy from abroad, and recoup a growing return from our large foreign investments, the excess is not large enough to offset the other factors.

It is easier to prescribe what not to do to get rid our deficits than it is to find the right combination of remedies. First, it is clear that the United States has rightly rejected devaluation of the dollar or any impairment of the inter-convertibility of gold and the dollar at the fixed price of \$35.00 per ounce. Such a step would be a breach of faith with our friends abroad, and with our own citizens, that would undoubtedly wreck the international financial structure we have been building since World War II. Incidentally, we have seen within recent years how disturbing to international confidence any tampering with fixed exchange rates can be. I am confident that none of the major nations will upset our world financial structure by seeking temporary competitive advantage through exchange rate adjustments and clearly such action is unthinkable in the case of the dollar.

Second, we should not take steps that run counter to our basic objective of unrestricted trade and investment flows. Of course the tying of our economic aid is somewhat vulnerable on this count but it can be justified as a temporary measure, facilitating special government transactions largely outside the ordinary commercial channels. Any form of exchange control, however, whether by legal restriction or by moral suasion, is clearly excluded if we adhere, as I am sure we will, to the sound principle of promoting a free flow of trade and payments.

Let me digress a moment. Many people have told me that they have heard that the Treasury, or the Federal Reserve Bank of New York speaking for the Treasury, has advised bond underwrites, insurance companies, commercial banks, or managers of pension funds not to extend dollar credits, or arrange for such extension, to foreign borrowers. To be sure, where large amounts are involved, we have always felt free to discuss with those concerned the timing of such payments, having in mind the desirability of avoiding undue market pressures. But I would like to emphasize as strongly as I can that we at the Federal Reserve and the Treasury have not interfered with private decisions to lend abroad nor raised objections as to amounts. These are private business decisions and they should remain so.

Having touched on what we should not do, let us turn to the possibilities that are open to us for a vigorous attack on our payments problem. First, with respect to increasing our exports and our favorable trade balance, the level of our costs and prices is crucial in the long run, and it is the long run that will count, since a major change in our export volume can hardly be achieved

overnight. We should welcome the efforts that are being made to get America more “export-minded”, to provide government assistance in finding markets, and to streamline our methods of export financing and insurance; but important as these aspects are, it is on the field of costs that the battle will be won or lost. In the past couple of years, sharp rises in European wage rates and attendant price increases have helped us to some extent, but it would be foolishly complacent to court on Europe to continue indefinitely this involuntary help. For one thing, rapidly rising productivity abroad is still working hard in the opposite direction; and besides, serious resistance to higher costs on the part of foreign governments and central banks is beginning to appear in a number of countries.

Some in this country argue that we needn't worry too much about costs but rather should push for faster growth, on the theory that a more active economy would automatically boost productivity and reduce costs. Much as I would welcome more rapid growth, I don't think we can count on this for “automatic” cost improvement. On the contrary, unless we consciously aim at vigorous cost control, higher business activity could reawaken the inflationary pressures that plagued us in the 1950s. Keeping wage and salary increases within the limits of national productivity gains would seem to be a minimal target in this area. Corresponding moderation is also essential in other cost elements, including executive compensation, as well as in pricing policies.

With respect to our Government financial commitments abroad, while I am encouraged by the reductions initiated or accomplished in the last year or two, a great deal more remains to be done. The tying of our economic aid is not a full answer to that source of dollar drains, since a part of the tied aid may well be used to buy goods that would have been purchased from us even in the absence of aid. Doubtless, further gains can be made in the area of sharing the aid burden more equitable with our friends abroad, even granting the difficulty of reaching agreement on fair yardsticks for sharing. I suspect that greater emphasis on multilateral aid would produce real long-run savings. I'm sure many of you have read with keen interest, as I have, the report of the President's Advisory Committee on Foreign Aid, and I am heartened by the attention being given to these proposals by the Government. I would also hope that the program of matching United States military spending abroad with foreign military purchases in this country will be pushed to the maximum. This, too, should result in meaningful savings of foreign exchange.

But even after all these have been done, we may still face the hard question whether we can afford all of the commitments we have taken on, or whether some of them which do not directly contribute to our military security should not be substantially reduced. In seeking an answer, we cannot forget that the widespread use of, and reliance on, a strong dollar by the entire free world is a vital part of our national strength, political as well as economic.

We come now to capital movements. Our efforts to sustain short-term interest rates over the past year or two have been helpful, but the outflow of short-term capital remains too large. Partly, this

outflow is due to the tendency of corporations, and sometimes banks, to take advantage of the higher rates obtainable abroad, often in the Euro-dollar market. Sizable outflows of long-term capital are also continuing. While the interest rate gap has been narrowed somewhat by declining rates in Europe in the past year or so, I am doubtful that we can count on further declines substantial enough to relieve us of this problem. I see no reason, for example, to believe that foreign monetary authorities will refrain from using restrictive credit measures to protect their currencies from the threat of cost or price inflation.

As I have already indicated, I am glad that our Government has taken a firm position against direct controls over capital flows. We should by all means continue our efforts to encourage further development of the European capital markets and a larger influx of foreign long-term capital into this country. However, this problem is not one that can be solved overnight by the removal of various remaining European government restrictions. A psychological heritage of inflation fears, scarcity of savings and heavy domestic capital needs all suggest that improvement in this direction will be relatively slow.

There remains, of course, the possibility of curbing the capital outflow through changes in our interest rates and credit availability. While this is, in a sense, “home territory” for the Federal Reserve System, I would hasten to add two caveats: (1) the level of interest rates and the availability of credit, especially long-term credit, depend importantly on the balance of savings and investment within this country, as well as on deliberate monetary policy. In the last year or

two, with our resources less than fully employed, there has been a distinct tendency for the supply of savings to outrun investment demands. (2) We must not, of course, lose sight of the effects of monetary policy on our domestic economy. Fortunately, we do not need to worry about having to make money any easier, in view of the country's present ample liquidity.

For several years now, monetary policy has walked a narrow path between international domestic considerations, and it will undoubtedly have to continue to do so. But I am convinced that what might appear to be a stark short-term conflict between domestic and international objectives disappears in the long run. There could be but a precarious gain in domestic activity if we do not surmount our long-run payments problem, while a vigorous domestic economy that attracted funds to these shores would contribute most importantly to achievement of balance in our international accounts. But in any case, as I have said on previous occasions, monetary policy must be prepared to act decisively in defense of the dollar if the need should become sufficiently acute.

Let me say a word about tax policy. Once we get away from the controversial details of the proposed program, I am impressed by the broad support for a reduction in both individual and corporate income tax rates as a means of removing a drag on our economy and improving the atmosphere for productive private investment. I have been bothered by the unduly sharp distinction drawn between tax reduction and tax reform, since it seems clear to me that the most needed reform is a reduction in tax rates. Apart from objections to the specific measures presented as reforms, most of the dissatisfaction with the tax program seems to reflect doubts as

to whether there has been enough restraint on the spending side. I have been encouraged by recent statements that defense and space outlays should reach a plateau in the next year or two. However, I am not at all sure that there could not be some further paring even in these two categories. And it is all too evident that some of the civilian programs are much larger than could be justified on sound economic grounds. Evidence of more effective limitation of total expenditures would, quite logically, facilitate wide acceptance of tax reduction.

Hopefully, tax reduction and the resulting stimulus to the economy would benefit our balance of payments, both by making investment in this country more attractive and by making U.S. funds somewhat more expensive and less readily available to foreign borrowers, as domestic demands for credit became more pressing. Moreover, tax reduction would free monetary policy from some of the burden it has been carrying of encouraging domestic business expansion, leaving it better able to respond promptly and flexibly to international strains on the dollar. I was gratified by Secretary Dillon's clear recognition of this pointing his excellent address to the ABA Monetary Conference in Princeton last month.

I have heard the objection that our foreign friends' confidence would be so shaken by the enlarged budget deficits resulting from tax cuts that we would lose the benefits to be gained in other directions. This view I cannot share. I believe that they would not be disturbed by a temporarily enlarged budget deficit, provided it was soundly financed, and that expenditures were

being brought under control. Under these conditions, they could expect an accompanying economic expansion and associated credit developments leading to a better payments balance.

Perhaps a word is in order here about Federal deficits in general. That a long series of substantial deficits should be avoided seems to be incontrovertible. There have been too many examples in history of inflation engendered by uncontrolled deficits to permit us to lose sight of the ever present threat of abuse. Having in mind the usual gap between targets and actual performance, we would be unwise to abandon the objective of balanced budgets over an extended period of time. But this is quite different from saying that a Federal deficit automatically spells inflation, present or future. As the experience of the last four years seems to have shown, much depends on the nature of demand or cost-push pressures in the economy arising from the combination of all relevant factors, both public and private. Moreover, the means of financing the deficit can be crucial. The 1962 experience in this regard was reassuring, and I am sure that neither the Federal Reserve System nor the Treasury could countenance an inflationary method of financing whatever enlarged temporary deficits may result from tax reduction.

I believe that a solution of our balance-of-payments problem can be found in some combination of actions along the lines that I have sketched this evening. A Good start, of course, has already been made on most of these measures. The harder steps lie ahead of us, but they are no less urgent on that account. We cannot have a vigorous and expanding economy, nor can we play a role in world affairs worthy of the United States, if the dollar becomes a weak currency. We still

have time for the right measures to become fully effective if we have the courage to see them through, and I firmly believe that we do.

#### QUESTION AND ANSWER PERIOD

QUESTIONER, ARMAND G. ERPF: “Mr. Hayes, while we have had international payment deficits for about a dozen years, the problem apparently only reached the upper echelons of government over the last three-four years”.

“Do you think that now, being aware of the problem, there is sufficient sense of urgency so the fundamental solutions are being sought, or are we and the dollar to hang indefinitely in a state of uncertainty”?

“Is not our policy too much the inevitability of gradualness”?

ALFRED HAYES: “I feel myself that the sense of urgency on this problem is increasing not only in the Federal Reserve Bank of New York, but throughout the country and particularly in Washington, which is after all the most important place for it to occur”.

“I’m very much encouraged by the tangible steps that have been taken already by our government and it seems to me quite clear that the balance of payments is receiving a pretty high priority. I—you know as much about some aspects of this as I do. You’ve all read about the gold

budget, so-called, of the government and the, we've read news releases today—I don't know any more than what I read in the ticker about Mr. McNamara's efforts but it seems to me that it's clear that it does enjoy high priority. I feel confident that we will find a solution soon; we must find a solution soon".

QUESTIONER, J. WILSON NEWMAN: "Mr. Secretary, first is a preliminary inquiry to my main question. In these troubled times when all of us have become very mindful of the importance of the public interest, and being aware of the seriousness of the talk which you have just delivered, I would like to know first sir if I should raise a few selective questions, is there any risk that I may say something prejudicial to national security"?

SECRETARY DEAN RUSK: "There's nothing embarrassing about questions. The answers might be embarrassing. (LAUGHTER) But you leave that to me. You go right ahead".

J. WILSON NEWMAN: "Well now, Mr. Secretary, in view of the fact that the – you have devoted practically all of your remarks to Vietnam and Laos, does this mean that these subjects rank high in importance facing this nation, or does it mean that on such matters as Cuba, Berlin and South America are further down the line or you'd rather not talk about them"?

SECRETARY DEAN RUSK: "No, not at all. I indicated (APPLAUSE) I indicated earlier that I do not wish to inhibit the questions in any way. I elected to use my 20 minutes to talk about a

particular subject cause I think that it's too easy to skip right across an entire range and I wanted to dig into at least one of them and one that is far away and not very well understood in this country in order to get into some of the anatomy of the problem”.

“But you are – I would welcome questions on any of these subjects you wanted to get into. You shoot the questions”.

J. WILSON NEWMAN: “Well obviously I thought I'd have a few minutes to think it up, sir.

(LAUGHTER) But to begin with, I wonder if you would state sir your understanding of the Monroe Doctrine and just what the policy of the United States is just now with respect to it”.

(APPLAUSE)

SECRETARY DEAN RUSK: “Well I think all of us know the tradition behind the Monroe Doctrine. We are more interested in half of it these days than we are in the other half, because we are deeply involved in European and other affairs which were eschewed by the Monroe Doctrine, but what is ever more important today is the treaty structure of the hemisphere, the security arrangements of the hemisphere in such things as the Rio Pact”.

“Now, as a matter of policy, as a matter of policy objectives, the hemisphere has unanimously agreed that a Marxist-Lenist regime in Cuba is incompatible with the institutions of the Western Hemisphere and that the aim must be to welcome a free Cuban people back into this

hemisphere”.

“Now as I pointed out just a few days ago in another, in another place, the actions that are now being taken fall into three main categories. The first has to do with the commitment of the armed forces of the United States and other armed forces in this hemisphere to accomplish certain purposes. One to insure that there not be introduced back into Cuba offensive weapons which will threaten the security of this hemisphere. Second, that they keep the kind of eye on Cuba, a watchfulness on Cuba to assure us that this is the case in that particular island. To insure that there is the safe and free use of international waters and airspace in the Caribbean area without interference from the island of Cuba. To insure that there will not be arms shipped from Cuba to other parts of the hemisphere illicitly against inter American orders or any other type of foray from Cuba against those other countries, and also to insure that there not be repeated in Cuba the situation which was demonstrated in Hungary some, some time ago about the use of Soviet arms to impose a political solution against the will of Cubans on the spot”.

“A second course of combination of actions has to do with insuring that this Marxist-Lenist regime does not offer any future for the Cuban people or any example for the rest of the hemisphere in terms of economic and social development. There’s been a drastic reduction in normal relations, economic fiscal and otherwise between Cuba and the rest of the free world”.

“This has to do with trade, with shipping, with all of the transactions which have to do with the

economy of the island. That is having an important impact upon the country inside the island and is raising the price rapidly for the other side if they try to maintain their present position there”.

“And a third set of actions has to do with the rest of the hemisphere to insure that any attempt from Cuba to send funds, personnel, agents into other countries will be interrupted and also and most important of all to insure that these other countries of the hemisphere and their peoples really understand that economic and social development and rapid economic and social development is something that is to be undertaken through free institutions and that it is the free world that has the more adequate answer for that solution”.

“I think the results of all of these steps in the hemisphere have been sharply to cut down on Castro’s, the bloom of Castro’s original revolution, I think he’s been abandoned throughout the hemisphere by all but the hard-core communist apparatus in country after country in by and large there are few, there are a few organizations that still seem to, to pay him some attention”.

“Now there remains the question of the presence of Soviet forces which we have indicated to the Soviet Union and have declared cannot be accepted as a normal state of affairs in this hemisphere”.

“Those forces have been moving out they, it is our purpose to see that they do continue that movement out and the question is how when under what circumstances. The presence of those

forces here is itself a source of danger, itself a major intrusion into the possibilities of relations between the West and the East on any kind of a normal basis, and is an irritant which, which ought to be, which ought to be removed”.

“Now there still remains the questions of invasion or a major act of war in dealing with that situation. Now let me say to you that if someone says to me I want to invade Cuba and take all the consequences of that step whatever they are I would honor you for an idea which at least has some inner integrity”.

“But let’s don’t kid ourselves that just waving missiles is going to cause the other side to roll over and play dead and if you want to do all sorts of drastic things on the, on the assumption that no shooting will result, just don’t entertain any such illusions”.

“It is necessary to incur very great risks in order to meet great threats, and that was demonstrated last October, and if anyone is under the impression that there was not a very great risk involved last October, then you must catch up to date with the facts”.

“But it is not my judgment that the threat in Cuba at the present time warrants the escalation of events and the escalation of violence which would be involved in direct military action against that island, and a direct military action of that sort is something for which we must remain responsible and which we must not leave in the hands of those who do not carry the

responsibilities which we do for our own people and for situations in other parts of the world”.

“So I would like to have those who want to do more about Cuba be more precise than the use of general language, because practically everything that can be done short of the use of armed forces is being done and is having very considerable effect. Thank you”. (APPLAUSE)

QUESTIONER, ARMAND G. ERPF: “Mr. Hayes, this question will neither be as broad nor as risky. It strikes me as roughly the dollar deficit problem has three facets: the private sector, the government sector, and the area of financial measures of technical competence and dexterity if not legerdemain. Is not the government sector the chief culprit in that military expenditures and grant-in-aid disbursements overseas are too heavy to be offset by the very favorable balance of the private sector? And is it not too much to expect that the technical brilliance of the Fed and the Treasury along can neutralize the erosion of the private position, which with taxes and costs difficult to curb or reduce, must bear the brunt of pentagon and State cash largess overseas, which not only adds to the burden of the deficit, but induces unemployment at home and over employment abroad”? (LAUGHTER)

ALFRED HAYES: “Well, let me—let me dispose of the third dimension first. You speak of the—the questioner speaks of the legerdemain of the Treasury and the Federal Reserve as a part of the total balance of payments problem. I wouldn’t recognize it as such. I tried—as I tried to point out in my speech, we have no thought that these measures represent any part of the

fundamental solution of the balance of payments. We do believe that they serve a very useful purpose in mitigating the immediate effects of the balance of payments deficit through relieving our gold stock of sudden drains or helping, reciprocally, other currencies that get in trouble in relieving their reserves of sudden drains”.

“We believe that it serves a very useful purpose, but it is not a part of the basic balance of payments problem”.

“Now, getting down to the question of what is—what are the principal components, you can if you wish break down the two—the balance of payments total of items into the public sector and the private sector. There are a great many ways of breaking down the balance of payments, and no one can say what item specifically causes the deficit because anyone can allocate any item he feels like as the cause of the deficit”.

“It might—I do think, however, that you can say we have what would normally be considered rather abnormally heavy burdens for our economic and military commitments abroad. But those have grown with the country, and we can’t shirk the fact that we do have these commitments, we do have these obligations abroad. As I said, I believe that we should be very careful in scrutinizing just how—how important they are, and we shouldn’t let ourselves be spread too thin or be—or waste our substance where it isn’t really pay dividends. I hesitate to talk about this in the presence of the Secretary because he knows so much better than I where or to what extent it

might be possible to reduce any of these commitments. But I can't help feeling that something can and should be done in that area".

"Now, I think that it's clear that in the area of private capital movement a great deal could be done. This—most people don't realize just how big that flow is, but if you take—the long-term capital movement abroad is approximately two and half billion dollars a year, private capital, and the short-term has been running in the last couple of years one and a half to two billion if you include errors and omissions, which is a nice euphonious way of talking about short-terms capital".

"Now, to get at those, obviously there is quite a problem, and I tried to bring out the fact that I don't believe you can get at them by direct control. I believe that in any attempt to do that you would—you would damage irreparably the system we're trying to construction and support. I do believe that there are alternative ways of checking those capital drains, and there are costs involved, and we have to weigh at all times the costs that are involved".

"There are costs perhaps in terms of the domestic economy. I—one reason I stepped out of the usual—departed from the usual tradition in the Federal Reserve System of not entering into tax questions is because I feel that the tax reduction program does have such a very direct and important bearing on what monetary policy could do to help the capital flow problem. I also pointed out that if the problem seems acute enough, monetary policy might have to act anyway".

“Now, then you come down to the question of what we have in the way of trade balance to meet these commitments, and I say—I give great credit to the private economy for what it has been able to do in the way of a favorable trade balance and a favorable balance of service items. The fact of the matter is that that’s a very big balance, running somewhere in the neighborhood of seven billion dollars a year, and the question arises should it be bigger? Well, I would like to see it bigger, and I like to see the efforts to make it bigger, but we must face the fact I think that it’s not easy in the face of the competitive situation in the world and the efforts of other countries to build exports to do very much on that side”.

“My--my own judgment would be that—and I think to that extent I’d agree with the questioner—we must to some extent take this ability to earn a favorable trade balance as a datum that can only be very gradually expanded , and we must do most of the remedying of the balance of payments on the side of the commitments”.

SECRETARY DEAN RUSK: “Mr. Chairman, may I buy just a little piece of that one”?

CHAIRMAN, GENERAL POWELL: “I was going to suggest it. Go right ahead”.

SECRETARY DEAN RUSK: “There’s no question whatever that in Washington we do look upon this balance of payments problem as a matter of major and urgent concern. It is also true

that a good part of the problem seems from the bookkeeping point of view to be involved in our defense and aid commitments abroad”.

“Now, there are a good many things that can be done on both those—those items. We can, we believe, get our allies to take more of a share both in defense and in foreign aid. Now, they have been improving their own performance in both those steadily. European aid, for example, to the continent of Africa is more than twice our own at the present time. And they’re showing considerable improvement in their own effort”.

“We in the meanwhile in foreign aid are trying to move as rapidly as possible to the proposition that what we have to offer in aid are goods and services originating in the United States, that free dollars—that is, dollars that involve the gold flow problem—are not to be considered a part of our aid program. It takes a little time to adjust to that. So we’re working at it from that point of view, and there’s been a sharp reduction in the impact of foreign aid on the total exchange situation”.

“But this is not something in which we can—which we can meet by simply reducing these commitments abroad because all sorts of other things begin to unravel. And I would like to urge the point that to the extent that we can increase our own exports of goods and services from this country on trade account, we are thereby contributing directly to our security requirements abroad and to the other great burdens that we have to undertake”.

“I think it is fair to say, and this is not—no new comments, that both business and government since 1945 went through a period of somewhat—of a relaxed attitude toward these matters. We were in a seller’s market. Now we’re moving into a new period of competition and the necessity for greater effort. We ourselves some months ago have gone to all of our embassies to our own ambassadors personally and reminded them that the promotion of trade was the first obligation of American diplomacy when Benjamin Franklin first set out on his trip to France in the 18<sup>th</sup> century, and that this is something that the ambassadors and everyone in their embassies must get hold of. And similarly, a new energy on the part of—additional energy on the part of business can help to win these credits that we need so badly for our—for our major commitments”.

“We are not at the point yet where we need to establish priority, and I do not wish in any way to throw any—to anticipate which is not in the minds of people in Washington. But I will put to you as a matter of priority: if you had to choose between withdrawing American forces from Europe, for example, and imposing some limitations on free decisions about private investments in Europe, which in the national interest would be more desirable”? (APPLAUSE)

ALFRED HAYES: “I’d like to just switch the question a little and say if the question—if the question were between withdrawing the dependents of forces in Europe or putting controls over capita exports, which would you choose”? (APPLAUSE)

CHAIRMAN, GENERAL POWELL: “We have time for one--two brief questions, one from

each interrogator”.

QUESTIONER, J. WILSON NEWMAN: “MR. Secretary, I feel it necessary to proceed very deliberately. Lest the candor of this forum be misinterpreted as hostility, let me hasten to say that businessmen as a group and businessmen in this room have a deep, heartfelt sympathy for the heavy responsibilities which you have and which you bear so well. But businessmen are exhorted from time to time in generalities, ‘increase your exports; work with the people abroad”.

“And I think it would be indeed very helpful, sir, if some of these generalities could be broken down into specifics and enumerate a few specific things that businessmen could do and a few specific things which they are doing now that they should not do”.

SECRETARY DEAN RUSK: “Well, I’d be—I’d be glad to do that provided it is understood that if I point one finger at you I’ve got three fingers pointed at myself here about things that we might do on our own side to help out. But I do think that we need to shorten the time lag between the discovery of a business opportunity abroad and its serious consideration by an American business who might be able to do something about it. I’m not at all sure that we get this news around, either through governmental or business circles, fast enough”.

“Now, one of our problems is simply this: that if we hear of a business opportunity in a particular country and we pick up—on the basis of a cable we pick up the phone and call a business and

say, “Look, here’s this opportunity. Why don’t you go after it’? We get into deep trouble because there are such things as competitors. And so this has to be circulated in trade journals. We don’t have the freedom of action of moving fast on this. This is circulated generally throughout the industry so that we do not become involved in getting in direct touch with one company rather than another in regard to a particular piece of business. Now whether there’s anything can be done about that I don’t know”.

“But I think also, and here let me go back before I came onto this particular job that I’m on now, go back to a period when I was a customer of American business and a good many countries overseas. I think that there have been indications that we have been somewhat slow to respond in such things as service, sales, spare parts attention, taking advantage of such things as air deliveries and things of that sort, compared to some of the other competitors in countries that have freshly arrived on the scene in the postwar period such as German and Ital and Japan. I think there are some improvements there”.

“To give you an example, which I think would—I know of one considerable exporter who has found that the very packaging of materials for shipment abroad has been so deficient that when he buys fro foreign export he brings them into his own warehouse and repackages before he ships them abroad. Well, I think we can do better”.

“You asked for some specifics? I think there are some specifics we can get into. But I think, Mr.

Chairman, that what we might do, might very well do, and I've talked to Luther Hodges about this, is to try to sit down in a group of people who are deeply involved operationally with this problem on both sides and have a hair-shirt talk in which each side can talk to the other one about how we can both get on with this job more effectively. And I think there are some things that we could do that would help in both directions. I'm sure you can tell us where we fail, but we might point out some of the problems that we've seen cropping up here and there".

"Let me say that I do think this: that there has been an enormous recovery of attitude, shall I say, on the part of American Enterprise with regard to foreign trade in the last very few years as competition has arisen from other sources. But it's going to require continual application of the dynamism which has characterized our free enterprise society if we are to keep up with the fast-growing competition which is coming in from other countries". (APPLAUSE)

ALFRED HAYES: "Might I just add one other specific: it seems to me we can take encouragement from the obvious fact that American business is more conscious of the need for remaining competitive in their cost structure. I hope that labor is becoming more conscious of it, too, but it seems to me that that, the consciousness on the part of those two big elements of the vital significance of cost in this whole export question, is absolutely crucial". (APPLAUSE)

SECRETARY DEAN RUSK: "In the event that there are some of you who are not aware of it, we have in the last few months established in the Department of State with close cooperation

with the Department of Commerce a business advisory group under Clarence Randall, whose job it is to help us follow through fast on situations in which American business find themselves in difficulty abroad. Now this has been working out to my own personal knowledge very well over the past three or four months, where it has been possible for us to come in in a timely fashion and give significant and serious assistance to a business that finds itself in some difficulty in a foreign country. And at the same time the other countries realize that we are going to be moving promptly on these things, and their own attitude toward American business I think has shown some improvement”.

QUESTIONER, ARMAND G. ERPF: “Now that the international payments problem if not solved has been plunked on the doorstep of private business, which will contend with taxes, labor costs and anti-trust attacks, and assuming that the problem is solved and we cease to have a significant or worrisome international payment deficit, do you think that the world can satisfactorily finance an expanding world trade, or will we face contraction and deflation? If so, what should be the basic approach: Ruse’s deals, Bornstein’s ideas, or the Trippen or Stamp plan? Or do you think that the Fed and the government will be prepared to cope with this new problem, or will we only get at it when crisis is upon us”?

ALFRED HAYES: “Quite a--quite a mouthful. (LAUGHTER) Well, let me start out by questioning whether deflation is a serious problem at the moments. I’m aware that some distinguished observers feel that it may be a problem around the corner. I have the feeling that

those who are looking at some of the under developed countries are more incline to get that impression than those who are looking at the highly industrialized countries. Having just returned from Europe and having seen how acutely worried they are in some of the principal countries there about the fact that wages have been going up about fifteen % a year, I can't feel the deflation is their primary problem at the moment".

"Now, as to the sufficiency of the means of payment to support a growing world economy, I personally see no evidence whatsoever that the means of payment regard as traditional won't be sufficient to meet these—these needs. The—for one thing, we can look at the gold situation. People frequently talk about the inadequacy of the gold supply. Actually the annual increment to the gold supply is quite generous. Last year there was a 7% increase in world production of gold. About a billion and a half dollars of gold becomes available each year, either to go into monetary stock or to go into private hoards".

"Another crucial point here is how can it be prevented from going into private hoards, and the only way I know of is to increase the confidence in the monetary units so that people can see the light and not waste their substance buying a wholly unproductive asset. I—I'm optimistic on that, and I believe that if e can achieve reasonable balance in the balance of payments, which is the premise you made, that we'd not only not see the amount of gold disappearing into hoards we've seen in the last two, three, four years, but we'd see probably quite a bit coming out of hoards".

“Secondly, in trying to estimate the amount of world liquidity, I think we—Perry Jacobsen has pointed out quite rightly that the crucial thing is how much you have to meet the big swings in credit. We—we don’t need a great—there are many countries now with reserves that are more than ample for any normal period. It’s only if they found themselves in severe crisis that they would need anything like that amount of reserves or supplemental resources. So it’s the availability of credit resources to meet big swings that to my mind is the key to sufficient world liquidity, and as long as we have not only the kind of bilateral arrangement that we’ve worked out, but also the very major bulwark of the International Monetary Fund with their enlarged lending resources, I have little doubt that the available reserves to be drawn upon including monetary reserves and these credit facilities, are ample to meet any foreseeable needs in the future. The time may come when we need some more grandiose and spectacular scheme, but it’s not now”. (APPLAUSE)