FORTY-EIGHTH

Annual Report

OF THE

BOARD OF GOVERNORS
of the Federal Reserve System

COVERING OPERATIONS FOR THE YEAR

1961

DIGEST OF PRINCIPAL FEDERAL RESERVE POLICY ACTIONS, 1961

Period	Action	Purpose of action
January	Limited net sales of U.S. Government securities from Federal Reserve portfolio to about $500 million. Member bank borrowing at Reserve Banks averaged only $50 million.	To encourage bank credit and monetary expansion by absorbing only part of seasonal inflow of reserve funds not otherwise offset by a large gold outflow.
February-August	Bought substantial amounts of U.S. Government securities with maturities over 1 year, following February 20 announcement that System open market operations would include securities outside the short-term area. These purchases were partly offset by net sales of short-term securities. Total System holdings of Governments increased about $700 million. Member bank borrowings averaged $75 million.	To encourage bank credit and monetary expansion while avoiding direct downward pressure on short-term interest rates, thereby moderating pressures on the U.S. balance of payments from outflow of short-term capital attracted by higher interest rates abroad.
September-December	Bought or sold at different times varying amounts of U.S. Government securities, including securities with longer maturities. Total System holdings of Government securities increased about $1.6 billion. Member bank borrowings at Reserve Banks remained generally low.	To continue to encourage bank credit and monetary expansion while allowing for changing reserve needs due to seasonal and other factors, including a large gold outflow, and while continuing to give consideration to the balance of payments problem.
December	Raised, effective Jan. 1, 1962, maximum interest rates payable by member banks on any savings deposit from 3 to 3½ per cent, and to 4 per cent on those left in the bank for 1 year or more; also raised maximum rates on time deposits with a maturity of 6 months to 1 year from 3 to 3½ per cent, and to 4 per cent on those deposits with a maturity of a year or longer.	To enable banks to compete more effectively for savings and other time deposits, including foreign time deposits, thus moderating pressures on the U.S. balance of payments, and, over the long run, to offer additional incentive for the accumulation of savings required for financing future economic growth.

out undue downward pressure being exerted on the short-term rate.

2. Authority to effect transactions in intermediate- and longer-term securities.

The Committee authorized the Federal Reserve Bank of New York, between this date and the next meeting of the Committee, within the terms and limitations of the directive issued at this meeting, to acquire intermediate- and/or longer-term U. S. Government securities, or to change the holdings of such securities, in an amount not to exceed $500 million.

> Votes for this action: Messrs. Martin, Hayes, Balderston, Irons, King, Mills, Shepardson, Swan, Szymczak, and Wayne. Votes against this action: Messrs. Allen and Robertson.

This action amended the special authorization first given at the meeting on February 7, 1961, by removing the restriction that had limited transactions to securities with a maturity of not more than 10 years, this removal having been recommended by the Ad Hoc Subcommittee that had been named at the meeting on January 10, 1961, to study and make recommendations with respect to the Committee's operating procedures. It was felt that the removal of the restriction on maturities would, by increasing the flexibility of Account operations, facilitate the evaluation of the feasibility and effect of System operations in other than the short-term market. The Ad Hoc Subcommittee also recommended, and the Committee agreed, that it would be desirable to take more time, during which the experience in operating in all maturities could be studied, before deciding on any possible revision of the Committee's operating policy statements.

Mr. Allen voted against continuing the special authorization on the same basis that he had previously dissented at the March 7 meeting. However, inasmuch as the authorization to operate in longer-term securities was being continued by majority vote, he did not object to the removal of the restriction against operating in maturities beyond 10 years.

Mr. Robertson had expressed at the February 7 meeting his reasons for dissenting from the proposals to carry on open market operations in other than short-term Government securities. He now dissented from the action to expand the original proposal not only on the basis of his conviction that the whole operation was unwise—the risks being too great to be offset or counterbalanced by the alleged potential benefits—but also because this proposal represented a further delegation of authority by the Committee to the Manager of the System Open Market Account without any plan or program to guide him in his operations. He did not believe that the Manager could be expected to carry out the Committee's unspecified objectives—whatever they were—solely on the basis of his own intuitions.

April 18, 1961

1. Authority to effect transactions in System Account.

At this meeting clause (b) of the first paragraph of the Committee's policy directive to the Federal Reserve Bank of New York was changed to provide that open market operations should be conducted with a view "to encouraging expansion of bank credit and the money supply so as to contribute to strengthening of the forces of recovery that appear to be developing in the economy, while giving consideration to international factors." The preceding directive, which had been in effect since October 25, 1960, called for operations with a view to encouraging monetary expansion for the purpose of fostering sustainable growth in economic activity and employment, while taking into consideration current international developments.

> Votes for this action: Messrs. Hayes, Allen, Balderston, Irons, King, Mills, Robertson, Shepardson, Swan, and Wayne. Votes against this action: none.

For some time open market policy had aimed at making a contribution toward arresting recessionary influences in the domestic economy, at the same time giving due regard to the level of short-term interest rates in view of problems related to the continuing deficit in the U. S. balance of payments. However, confirmation of a bottoming out of the recessionary phase of the business cycle had been gradually emerging. Statistical information suggested increasingly that the low point had been passed and that an upturn was in the making, although evidence of the prospective strength of the expansion was as yet lacking.

Data before the Committee showed that economic gains in March were moderate and that activity in some sectors had, in fact, continued to drift downward. Nevertheless, a number of key indicators showed significant improvement, after allowing for the usual seasonal influences. Among other things, personal income increased at an annual rate of $3.5 billion, housing starts were up for the third consecutive month, automobile sales strengthened, and exports appeared to be holding at unusually high levels. Although the level of unemployment continued to present a serious problem, particularly in certain areas, initial unemployment compensation claims recently had declined more than seasonally, and there were other signs of improvement in the labor market.

On the financial side, no significant changes in either the level or structure of interest rates had occurred since mid-March, most rates having remained a little above the lowest levels and well below the highest levels of the current calendar year. Total bank loans and investments had declined since the middle of March, perhaps more than seasonally. However, the money supply, defined in terms of demand deposits and currency, increased in the latter part of March and had since been maintained at the higher level then reached. In addition, holdings by the public of time deposits and comparable liquid assets continued to expand. The schedule of new corporate capital issues for April was heavy, and State and local government offerings continued reasonably large. Common stock prices had risen to record levels, with heavy trading, and stock market credit had expanded significantly.

The relatively high levels of unutilized human and physical resources continued to be of concern and suggested that there

was little prospect of serious inflationary pressures. The country's international financial position remained in moderate deficit, although gold movements in and out of U. S. monetary stocks had recently been negligible.

The change in the Committee's policy directive was deemed appropriate in recognition of the new phase of the business cycle into which the nation's economy appeared to have entered, even though the configuration of the recovery could not as yet be forecast. As to monetary policy, the pattern that the Committee had been following in the past few months still appeared suitable, and revision of the directive carried with it no intent to modify open market policy in any significant respect at this stage. For the period until the next meeting, it was the consensus that the directive should be implemented by open market operations aimed at maintaining approximately the same degree of ease that had prevailed for the past several weeks. In the majority view, such a degree of ease would serve to promote the objective, as stated in the directive, of encouraging the expansion of bank credit and the money supply. Because of the continuing uncertainties in regard to the balance of payments, the consensus also contemplated that attention would continue to be paid to the general level of short-term interest rates.

Three members of the Committee, Messrs. Balderston, Robertson, and Swan, dissented from the majority view on implementation of the directive. Mr. Balderston, who 3 weeks earlier had suggested probing toward a somewhat greater availability of reserves in order to encourage further expansion of the money supply, felt that despite the gain since mid-March a longer period was required to permit a conclusion that the money supply was rising fast enough to provide adequate liquidity. Thus, being uncertain whether the current level of reserves was sufficient to induce a satisfactory expansion in the money supply, he continued to favor moving the level of reserves somewhat higher. Mr. Swan also continued to feel that it would be desirable in current circumstances to follow a slightly easier reserve policy whenever market opportunities arose. Mr. Robertson felt that to continue to supply reserves only in the amounts that had been available in recent weeks would not be adequate to encourage or support credit and monetary expansion conducive to an early return to fuller utilization of human and material resources. He believed the risk that additional reserves might cause a decline in short-term rates and encourage a movement of funds from this country, with an accompanying loss of gold, was likely to be much less than it had been in the past.

2. Authority to effect transactions in intermediate- and longer-term securities.

The Federal Reserve Bank of New York was authorized, between this date and the next meeting of the Committee, within the terms and limitations of the directive issued at this meeting, to acquire intermediate- and/or longer-term U. S. Government securities of any maturity, or to change the holdings of such securities, in an amount not to exceed $500 million.

> Votes for this action: Messrs. Hayes, Balderston, Irons, King, Mills, Shepardson, Swan, and Wayne. Votes against this action: Messrs. Allen and Robertson.

Renewal of this special authorization, first granted on February 7, 1961, and amended on March 28 to permit operations in U. S. Government securities of all maturities, reflected the conclusion of the Committee that further operations outside the short-term market in pursuance of the objectives stated when the authorization was granted would be desirable. Messrs. Allen and Robertson dissented for reasons they had previously expressed.

May 9, 1961

1. Authority to effect transactions in System Account.

The Federal Open Market Committee made no change at this meeting in its policy directive providing that open market operations should be conducted with a view to encouraging expansion of bank credit and the money supply so as to contribute to

strengthening of the forces of recovery that appeared to be developing in the economy, while giving consideration to international factors.

> Votes for this action: Messrs. Hayes, Allen, Balderston, Irons, King, Mills, Robertson, Shepardson, Swan, and Wayne. Votes against this action: none.

From data presented at this meeting, economic recovery appeared to be proceeding more rapidly than had generally been anticipated, and at least as fast as the more optimistic forecasts had predicted it would. All available evidence pointed toward an increase in gross national product during the second quarter of the year. Preliminary data indicated that the Board's industrial production index for April would be up 3 points from the first quarter low of 102. In addition, schedules for steel and automobile production seemed virtually to assure some further rise in the index during May—perhaps enough to erase at least half of the 8-point decline from 110 in July 1960. Retail sales during April had been demonstrating strength, including sales of domestically produced automobiles, which had risen sharply in March from the depressed midwinter level. Dealer stocks of automobiles, which had been brought down somewhat in March from the relatively high levels that prevailed during the past year, had fallen further, and used car stocks were down sharply from a year earlier. Latest information regarding plant and equipment expenditure plans for 1961 indicated a decline of only 1 per cent from 1960, an improvement over indications of similar surveys made earlier in this year and in the fall of 1960. In the price area, consumer and wholesale prices generally had been stable, while sensitive commodities had moved up. On the other hand, in spite of the apparently growing strength of the economy, seasonally adjusted unemployment in April remained at about the midwinter high.

In the financial area, short-term interest rates declined somewhat in April and early May, while intermediate- and long-term rates showed marked declines except in the corporate market, where there had been an unusually large volume of new financ-