FORTY-NINTH

Annual Report

OF THE

BOARD OF GOVERNORS
of the Federal Reserve System

COVERING OPERATIONS FOR THE YEAR

1962

Period	Action	Purpose of action
January-February	Reduced System holdings of U. S. Government securities by about $500 million through net sales and redemptions. Member bank borrowings from the Reserve Banks averaged less than $100 million.	To permit further bank credit and monetary expansion by absorbing only part of seasonal inflow of reserve funds, mainly from post-holiday return of currency from circulation, while minimizing downward pressures on short-term interest rates.
February	Authorized open market transactions in foreign currencies.	To moderate and offset short-term pressures on the dollar in the foreign exchange market.
March-mid-June	Increased System holdings of U. S. Government securities by about $1.3 billion, of which half represented purchases of securities with maturities of more than 1 year. Member bank borrowings from Reserve Banks continued to average less than $100 million.	To promote further bank credit and monetary expansion while avoiding sustained downward pressures on short-term interest rates.
Mid-June-late October	Increased System holdings of U. S. Government securities by about $200 million with net sales and redemptions of Treasury bills of about $700 million being more than offset by purchases of coupon issues, of which two-thirds were issues maturing in more than 1 year. Member bank borrowings from Reserve Banks averaged less than $100 million.	To permit moderate increase in bank credit and money supply while avoiding redundant bank reserves that would encourage capital outflows, taking into account gradual improvement in domestic economy and possibilities for further advance, while recognizing the bank credit growth of past year and continuing adverse balance of payments.
July	Reduced margin requirements on loans for purchasing or carrying listed securities from 70 to 50 per cent of market value of securities.	To take into account the recent sharp reduction in stock market credit and the abatement in speculative psychology in the stock market.
October	Reduced reserve requirements against time deposits from 5 to 4 per cent, effective October 25 for reserve city banks and November 1 for other member banks, thereby releasing about $780 million of reserves.	To help meet seasonal needs for reserves, while minimizing downward pressures on short-term interest rates, and to provide for the longer-term growth in bank deposits needed to facilitate the expansion in economic activity and trade.
Late October-December	Increased System holdings of U. S. Government securities by about $1.0 billion, with more than half of the net increase in issues maturing in more than 1 year. Member bank borrowing from the Reserve Banks rose gradually over period, but only to an average of about $200 million.	To help further in meeting seasonal needs for reserve funds while encouraging moderate further increase in bank credit and the money supply and avoiding money market conditions unduly favorable to capital outflows internationally. In mid-December open market operations were modified to provide a somewhat firmer tone in money markets and to offset the anticipated seasonal easing in Treasury bill rates.

had passed their sustainable peak. He saw a serious threat to the domestic economy, which he felt should be recognized by supplying reserves somewhat more freely, by making it clear that there was no possibility of a discount rate increase under current conditions, and by being prepared to see the short-term rate decline by as much as half of a percentage point.

August 21, 1962

Authority to effect transactions in System Account.

Domestic economic developments in July, as reviewed by the Committee at this meeting, were more favorable than those in the immediately preceding months, and somewhat more favorable than had been suggested by evidence available at the preceding meeting of the Committee. Available data indicated widespread, if moderate, gains in activity. The industrial production index rose nearly a full point; new orders received by durable goods manufacturers rebounded sharply; and personal income, retail trade, and other important measures showed increases. Scattered figures for early August suggested that the July gains in production and sales were being maintained. On the less favorable side, housing starts failed to reverse the drop of June, and final figures for manufacturers' capital appropriations confirmed the sharp second-quarter curtailment that had been reported earlier. Also, while the seasonally adjusted rate of unemployment dropped slightly further in July to 5.3 per cent of the civilian labor force, the lack of growth in the labor force itself was viewed as a cause for concern.

Business loans at banks had apparently expanded somewhat in recent weeks, but the over-all private demand for bank credit continued to be relatively moderate. Required reserves and the money supply both declined in the first half of August, and there was a marked slowdown in growth of time deposits other than savings accounts. Yields on intermediate- and longer-term Treasury securities, which had risen in late June and early July, had declined substantially in the period since the end of July, and

heightened investor interest was apparent in all instruments from Treasury bills to long-term corporate bonds. One reason for the previous advance in yields had been the widespread belief that an early tax cut and a consequent substantial expansion of Federal debt were distinct possibilities. Correspondingly, a major factor in the decline in yields was the fading of this prospect, particularly after the President's statement on tax policy a week before the meeting. The Treasury was reported to be considering undertaking an advance refunding shortly after Labor Day, in view of the currently favorable market circumstances.

International payments of the United States in July were affected favorably by advance debt repayments on the part of France and Italy, and in July and early August were affected unfavorably by the reflux of funds to Canada. After allowance for these extraordinary factors, it appeared that the deficit in the payments balance was running at a rate smaller than in the third quarter of 1961 but larger than had been expected for the third quarter of 1962. It appeared to be at least as high as the adjusted second-quarter deficit, which also had been in excess of advance estimates. However, the position of the dollar in foreign exchange markets appeared to have improved somewhat, and private demand for gold in the London market evidently had declined.

In sum, recent domestic developments appeared moderately encouraging while those with respect to the balance of payments were disappointing; there continued to be substantial room for improvement on both fronts. A majority of the Committee concluded that, on balance, circumstances warranted a continuation of recent monetary policy. Accordingly, the following current policy directive, which reflected no change from the previous directive except to eliminate references to unsettled behavior in financial markets in view of the steadier performance of those markets, was issued to the Federal Reserve Bank of New York:

It is the current policy of the Federal Open Market Committee to permit the supply of bank credit and money to increase further, but at the same time to avoid redundant bank reserves that would encourage capital

outflows internationally. This policy takes into account, on the one hand, the gradualness of recent advance in economic activity and the availability of resources to permit further advance in activity. On the other hand, it gives recognition to the bank credit expansion over the past year and to the role of capital flows in the country's adverse balance of payments.

To implement this policy, operations for the System Open Market Account during the next 3 weeks shall be conducted with a view to providing moderate reserve expansion in the banking system and to fostering a moderately firm tone in money markets.

Votes for this action: Messrs. Martin, Balderston, Bryan, Deming, Fulton, King, Mills, Shepardson, and Treiber. Votes against this action: Messrs. Mitchell and Bopp.

Messrs. Mitchell and Bopp dissented because they would have preferred a directive indicating a greater willingness to encourage monetary expansion, substantially like that adopted at the meeting of May 29, 1962. They thought that monetary policy could make a greater contribution to economic expansion without risking significantly adverse effects on the balance of payments. In their opinion, the virtual elimination of any prospect for a Federal tax cut in 1962 increased the importance of adopting a more stimulative monetary policy. Mr. Mitchell also expressed concern about the lack of growth in the money supply since November 1961 which, he felt, had interfered with economic expansion. In his view there had been no monetary expansion since late 1961. The rise in time deposits and total bank assets that had taken place thus far in 1962 was due to the growth of banks as savings institutions or financial intermediaries and not to monetary creation brought about by Federal Reserve policy. Recent policy, therefore, implicitly denied the need for the money supply to grow with an expanding economy.

September 11, 1962

Authority to effect transactions in System Account.

It appeared that the improved performance of the economy in July was not continuing. Reports to the Committee at this meet-

ing, based partly on preliminary estimates, indicated that industrial production and retail sales had leveled off in August. Also, the seasonally adjusted unemployment rate had risen to 5.8 per cent, although this was reportedly due in part to special or technical influences. Surveys of consumer buying intentions and of business plans for inventory restocking and capital outlays suggested little change or only moderate gains in spending over the coming months.

After contracting in July, bank credit expanded markedly in August and grew slightly further in early September. Nevertheless, private demand deposits declined substantially in August. Treasury balances remained unusually high, and time and savings deposits at commercial banks continued to grow but at their recently reduced pace. The conventionally defined private money supply was at a level about 1 per cent below that at the end of 1961, after allowance for usual seasonal variations.

Long-term security yields were steady in early September, after declining during much of August. An advance refunding operation undertaken by the Treasury was still in progress at the time of the meeting, with early indications that it was being well received.

The international economic scene was reported to have changed little in recent weeks, with the deficit in the U.S. balance of payments about the same in August as in July (after allowing for the sizable foreign debt prepayments in July). Preliminary figures for late August and early September suggested some improvement, but it was too early to tell whether they indicated a trend.

A majority of the Committee concluded that, in view of continued evidence of adequate domestic liquidity and continuing indications of unsatisfactory progress with respect to the balance of payments, monetary policy should remain unchanged for the next 3 weeks. It was recognized that maintenance of the same general atmosphere of credit availability might require somewhat larger amounts of bank reserves than earlier, because of the concentration of money market pressures arising from large