FIFTY-FIRST

Annual Report

OF THE

BOARD OF GOVERNORS
of the Federal Reserve System

COVERING OPERATIONS FOR THE YEAR

1964

DIGEST OF PRINCIPAL FEDERAL RESERVE POLICY ACTIONS IN 1964

Period	Action	Purpose
January–mid-August	Increased the System's holdings of U.S. Government securities, after having reduced them seasonally early in the year. On balance, total holdings rose about $1.1 billion, $300 million of which represented net purchases of securities with maturities of over 1 year. Member bank borrowings averaged about $275 million.	To provide for moderate growth in the reserve base, bank credit, and the money supply for the purpose of facilitating continued expansion of the economy while fostering improvement in the capital account of U.S. international payments, after offsetting seasonal downward pressures on short-term interest rates early in the period.
Mid-August–late November	Increased the System's holdings of U.S. Government securities by about $1.5 billion, of which $600 million represented net purchases of securities with maturities of more than 1 year. Member bank borrowings averaged about $350 million.	To maintain slightly firmer conditions in the money market with a view to minimizing the outflow of funds attracted by higher short-term interest rates abroad while offsetting reserve drains and providing for growth needs of the domestic economy.
Late November	Raised discount rates from 3½ to 4 per cent. Raised maximum interest rates payable on savings deposits held for less than 1 year from 3½ to 4 per cent and those on other time deposits from 4 to 4½ per cent for maturities of 90 days or more and from 1 to 4 per cent for maturities of 30-89 days.	To counter possible capital outflows that might be prompted by any widening spread between money market rates in this country and the higher rates abroad, following a rise in official and market rates in London, while at the same time ensuring that the flow of savings to commercial banks remains ample for the financing of domestic investment.
Late November–December	Increased the System's holdings of U.S. Government securities by about $765 million, part of which represented securities acquired under repurchase agreements. Member bank borrowings averaged about $275 million.	To offset seasonal reserve drains and to accommodate further moderate expansion in aggregate bank reserves while ensuring that the rise in money market rates following the discount rate actions did not restrict the availability of domestic credit.

currencies in accordance with the Guidelines on System Foreign Currency Operations reaffirmed by the Federal Open Market Committee on March 5, 1963, as amended May 28, 1963; provided that the aggregate amount of foreign currencies held under reciprocal currency arrangements shall not exceed $2.05 billion equivalent at any one time, and provided further that the aggregate amount of foreign currencies held as a result of outright purchases shall not exceed $150 million equivalent at any one time:

Pounds sterling
French francs
German marks
Italian lire
Netherlands guilders
Swiss francs
Belgian francs
Canadian dollars
Austrian schillings
Swedish kronor
Japanese yen

The Federal Reserve Bank of New York is also authorized and directed to operate in any or all of the foregoing currencies in accordance with the Guidelines and up to a combined total of $150 million equivalent, by means of:

(a) purchases through forward transactions, for the purpose of allowing greater flexibility in covering commitments under reciprocal currency agreements;
(b) purchases and sales through forward as well as spot transactions, for the purpose of utilizing its holdings of one currency for the settlement of commitments denominated in other currencies; and
(c) purchases through spot transactions and sales through forward transactions, for the purpose of restraining short-term outflows of funds induced by arbitrage considerations.

The Federal Reserve Bank of New York is also authorized and directed to make purchases through spot transactions, including purchases from the U.S. Stabilization Fund, and concurrent sales through forward transactions to the U.S. Stabilization Fund, of any of the foregoing currencies in which the U.S. Treasury has outstanding indebtedness, in accordance

with the Guidelines and up to a total of $100 million equivalent. Purchases may be at rates above par, and both purchases and sales are to be made at the same rates.

This directive was amended on two occasions during the year, as noted in entries for October 20 and November 24. The effects of the amendments were to specify an additional purpose for which forward transactions in foreign currencies were authorized and to modify the amounts of the dollar limits specified for foreign currency operations.

January 7, 1964

1. Authority to effect transactions in System Account.

As 1963 ended, economic activity was continuing to advance at a moderate pace, consumer prices were rising slowly further, and wholesale prices were little changed at about the level that had prevailed for 6 years. The unemployment rate had been relatively stable for 2 years; in 1963 it averaged 5.7 per cent of the civilian labor force and in 1962, 5.6 per cent. Stock market prices were at record levels, and interest rates on Government securities and high-grade corporate and municipal bonds were higher than a year earlier. For example, yields on longer-term high-grade bonds were up ⅛ to ¼ of a percentage point, and yields on 3-month Treasury bills were about ⅝ of a point higher. Not all interest rates had advanced, however; in particular, mortgage yields were little changed from their April levels and were below those of December 1962. Recent estimates suggested that the deficit in the U.S. balance of international payments was reduced appreciably in the second half of 1963 to an annual rate of about $1½ billion, and that the deficit for the year as a whole might have been below $3 billion. While still large, this would be the smallest deficit for any year since 1957.

Gross national product in the fourth quarter of 1963 was unofficially estimated at a $597-598 billion annual rate, 5½ per cent above a year earlier. Much of the recent strength in activity was attributable to high levels of consumer spending. After a slight dip in November, retail sales increased substantially to a record volume in December, as gains were recorded in all durable and most nondurable categories.

Business spending continued relatively cautious despite reportedly widespread optimism about the outlook. There had been some increase in the rate at which manufacturers increased inventories in October and November, but a survey indicated that they planned to reduce the rate of inventory accumulation in the first quarter of 1964. Business plans for fixed capital outlays called for little change from the record fourth-quarter level in the first quarter of the new year and a modest rise in the second quarter.

In the financial area, bank credit expansion in December was substantially smaller than in November, according to preliminary estimates. The seasonally adjusted money supply changed little from the first half of November to the first half of December, and growth in time and savings deposits appeared to have slackened markedly in December. Free reserves averaged about $150 million in the final 4 weeks of the year, compared with a little over $100 million in the preceding 4 weeks. Money market conditions on the whole were steadier than usual for this season of the year.

Yields on 3-month Treasury bills had fluctuated in a narrow range in December and early January, holding slightly above the 3½ per cent discount rate on most days in that period. Treasury note and bond yields edged up to new 1963 highs before leveling off late in December, and corporate bond yields reached their highest levels in over a year at the end of that month. It was reported that the Treasury might forego part of its anticipated January cash financing because of an unexpectedly strong cash position, and that it was actively considering an advance refunding in the immediate future.

Tentative weekly figures on U.S. international payments in

December indicated a surplus of about $450 million in that month, and implied a fourth-quarter deficit at an annual rate even below the reduced third-quarter figure. While part of the December surplus may have represented temporary transfers of funds for window-dressing purposes, trade figures through November suggested that some of the recent improvement in the payments balance was due to higher exports. On the other hand, outstanding short-term bank loans to foreigners increased sharply in October and November.

Economic activity abroad continued to expand. Inflationary developments appeared to be threatening in a number of European countries and continued to be evident in less developed areas.

The Committee agreed that no change should be made in its monetary and credit policy at this meeting, although several members indicated that they would have favored some shift toward less ease at this time on both domestic and international grounds if Treasury financing had not been in immediate prospect. These members felt that the recent rates of growth in bank reserves, bank credit, money supply, and nonbank liquidity were greater than justified by the needs of the domestic economy and had contributed to the large volume of foreign lending by U.S. banks. They also noted that rising foreign interest rates associated with efforts of the authorities in several countries to curb domestic inflationary pressures might induce increased short-term capital outflows. Even taking the Treasury financing into account, these members felt that it would be appropriate to reduce free reserves from the somewhat higher levels of recent weeks and to counter any downward seasonal pressures on short-term interest rates.

Other members, emphasizing the absence of boom conditions and psychology, the continued high level of domestic unemployment, the broad stability of commodity prices, and the recent improvement in the payments balance, felt that a shift to less ease would be undesirable even apart from the prospective

Treasury financing; they preferred to continue the current monetary policy as long as these circumstances obtained. For the immediate future, they saw no objection to somewhat lower short-term rates arising from seasonal or other market forces. Some members expressed the view that excessive stability in Treasury bill rates was undesirable on its own account.

The Committee's current economic policy directive to the Federal Reserve Bank of New York, as issued at this meeting, differed from that in effect at the beginning of the year only by the addition of a reference to Treasury financing in the second paragraph. It read as follows:

It is the Federal Open Market Committee's current policy to accommodate moderate growth in bank credit, while maintaining conditions in the money market that would contribute to continued improvement in the capital account of the U.S. balance of payments. This policy takes into consideration the fact that domestic economic activity is expanding further, although with a margin of underutilized resources, and the fact that the balance of payments position is still adverse despite a tendency to reduced deficits. It also recognizes the increases in bank credit, money supply, and the reserve base of recent months.

To implement this policy, and taking into account prospective Treasury financing, System open market operations shall be conducted with a view to maintaining about the same conditions in the money market as have prevailed in recent weeks, while accommodating moderate expansion in aggregate bank reserves.

Votes for this action Messrs. Martin, Hayes, Balderston, Bopp, Clay, Daane, Mitchell, Robertson, Scanlon, Shepardson, and Shuford. Vote against this action: Mr Mills.

Mr. Mills dissented from this action because he believed that a somewhat more liberal provision of reserves would yield beneficial economic returns, without complicating the Treasury's financing program.

2. Amendment of continuing authority directive.

On recommendation of the Account Manager, Section 1(a) of the continuing authority directive to the Federal Reserve

Bank of New York was amended to raise from $1 billion to $1.5 billion the limit on changes in holdings of securities in the System Open Market Account between meetings of the Committee. With this amendment, Section 1(a) read as follows:

(a) To buy or sell U.S. Government securities in the open market, from or to Government securities dealers and foreign and international accounts maintained at the Federal Reserve Bank of New York, on a cash, regular, or deferred delivery basis, for the System Open Market Account at market prices and, for such Account, to exchange maturing U.S. Government securities with the Treasury or allow them to mature without replacement; provided that the aggregate amount of such securities held in such Account (including forward commitments but not including such special short-term certificates of indebtedness as may be purchased from the Treasury under paragraph 2 hereof) shall not be increased or decreased by more than $1.5 billion during any period between meetings of the Committee.

Votes for this action: Messrs. Martin, Hayes, Balderston, Bopp, Clay, Daane, Mills, Mitchell, Robertson, Scanlon, Shepardson, and Shuford. Votes against this action: None.

January 28, 1964

Authority to effect transactions in System Account.

Information available at this meeting confirmed earlier indications that the domestic economy had ended the year 1963 on a strong note, and scattered data for January suggested that activity was continuing to expand. GNP in the fourth quarter was now estimated at a $600 billion annual rate, a little higher than previous estimates. Prospects for a Federal income tax reduction early in 1964 recently had improved. However, businessmen's announced spending plans suggested quiet optimism rather than exuberance, and a substantial volume of unutilized resources was still available for further expansion.

Industrial production increased about one-half of a percentage