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.

tion to investors expecting to make tax and dividend payments in that month and having particular liquidity needs in the closing weeks of the year. Bond markets displayed a more hesitant and cautious tone, and yields rose somewhat. Among the contributing factors were heavy inventory positions of dealers in Government securities and municipal issues and the build-up in the September calendar of new corporate and municipal public offerings from the seasonally low level of the summer. The rise in Treasury bond yields was modest partly because substantial Federal Reserve and other official buying had helped to relieve the overhang of supply in the market, but recent new issues of corporate bonds were priced to yield about 10 basis points more than they had a month earlier.

On the basis of preliminary data for August, the deficit in the U.S. balance of payments for July and August combined appeared to be running appreciably above the $3 billion annual rate of the second quarter. However, capital outflows moderated in July; short-term claims on foreigners reported by banks declined, partly offsetting a large rise in June, and outflows on long-term bank loans continued modest.

The Committee concluded that the policy decision taken at the previous meeting should not be altered in the light of the information on domestic and balance of payments developments that had become available in the interim. Accordingly, it was agreed that operations should continue to be directed toward maintaining the slightly firmer conditions in the money market that had prevailed in recent weeks. The following current economic policy directive was issued to the Federal Reserve Bank of New York:

It is the Federal Open Market Committee's current policy to accommodate 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, and seeking to avoid the emergence of inflationary pressures. This policy takes into account the continued orderly expansion in economic activity, some slackening in the rate of money supply

expansion in recent weeks, and relative stability in broad commodity price averages. It also gives consideration to indications that the deficit in the U.S. balance of payments was appreciably larger in July and August than in the preceding quarter.

To implement this policy, System open market operations shall be conducted with a view to maintaining the slightly firmer conditions in the money market that have prevailed in recent weeks, while accommodating moderate expansion in aggregate bank reserves.

Votes for this action: Messrs. Balderston, Hickman, Mills, Mitchell, Robertson, Shepardson, Shuford, Swan, Wayne, and Treiber. Votes against this action: None.

September 29, 1964

Authority to effect transactions in System Account.

The industrial production index advanced nearly one point further in August, and early indications were that it would show another rise in September. Nonfarm employment increased only slightly in August as temporary layoffs due to auto model changeovers reduced manufacturing employment. Retail sales in the third quarter were running about 2 per cent above the second-quarter level, and it appeared that the unusually high rate of personal saving of the period immediately following the March income tax cut had slackened. While the increase in business inventories thus far in 1964 was considerably less than had been indicated by prior surveys of business anticipations, more recent surveys suggested a higher rate of inventory accumulation in the months ahead.

Not all recent economic indicators were expansive. Private housing starts had been declining irregularly since late 1963, and in the June-August period they averaged one-eighth below the peak levels of last fall. New orders for manufacturers' durable goods dropped sharply in August, mainly because of a decline in defense orders, although they still were at a high level.

Average wholesale prices of industrial commodities continued stable, as increases for nonferrous metals and some other products were about offset by decreases elsewhere. New 3-year labor contracts entered into by two major automobile companies involved settlements above the administration's recommended wage guideposts, but whether these settlements posed a significant threat to continued over-all price stability was uncertain. It appeared that much would depend on the extent to which the terms of these contracts influenced settlements in other industries, and on the effects that they might have on price expectations and incentives for speculative inventory accumulation.

Bank credit rose substantially further in early September following a large increase in August. Credit extensions to finance corporate tax and dividend payments accounted for a significant part of the September increase. Advance estimates suggested that the money supply rose more in September than in August, and perhaps as much as in June and July when the increase was at an annual rate of 8.5 per cent. Growth in time and savings deposits in September was about in line with the average for the year to date, as gains in savings deposits were partly offset by the mid-September reduction in negotiable time certificates of deposit outstanding.

Member bank borrowings rose somewhat further, averaging $370 million in the 4 weeks ended September 23, as compared with $310 million in the preceding 4 weeks. Excess reserves also rose, but less than borrowings, and free reserves declined a little to an average of $80 million.

Conditions in the money market had firmed somewhat in recent weeks, and the interest rate on 3-month Treasury bills had advanced several basis points to 3.54 per cent. Bond yields continued to rise in early September, but after the middle of the month yields on Treasury bonds moved down; and somewhat later, yields on new corporate issues also declined. Dealer inventories of Treasury bonds had been reduced substantially from earlier levels.

More complete statistics on the U.S. balance of payments in August and tentative data for September indicated that the deficit in both months was below the high total for July. These data also suggested that for the third quarter as a whole the deficit might be somewhat less than that for the second quarter, which was now estimated at an annual rate of $2.7 billion. There was no evidence at present of net outflows of short-term capital in the third quarter, but outflows of long-term private capital apparently were appreciably higher than earlier in the year.

It was the consensus of the Committee that the slightly firmer money market conditions maintained under the directives issued at the two preceding meetings remained appropriate. Some members expressed concern about the possibilities for inflationary developments that they saw in the auto wage settlements and in the recent rapid growth rates in bank credit and the money supply, and about the continuing large deficit in the U.S. balance of payments. Another possible source of imbalance noted was the reported acceleration in demand for steel products resulting from fears of a work stoppage in that industry next spring. While no members favored a substantial change in policy, there was some sentiment for a further slight shading of market conditions in the direction of firmness, or at least for resolving any doubts that arose in implementing policy on the side of firmness rather than ease. The majority did not favor such a course, on the grounds that it was not warranted by price developments to date and that even a slight further lessening of ease in the money market might, under present circumstances, have large undesired effects on security prices and credit terms.

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national payments, and seeking to avoid the emergence of inflationary pressures. This policy takes into account the continued orderly expansion in economic activity, relative stability in broad commodity price averages, and indications that the money supply is expanding rapidly again after some slackening in August and early September. It also gives consideration to current estimates that the deficit in the U.S. balance of payments in the third quarter continued at a high rate, although possibly not as high as in the preceding quarter.

To implement this policy, 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, Daane, Hickman, Mills, Mitchell, Robertson, Shepardson, Swan, Wayne, and Bryan. Votes against this action: None.

October 20, 1964

1. Authority to effect transactions in System Account.

Underlying domestic economic conditions apparently continued strong in recent weeks, although new uncertainties were introduced by recent political developments abroad and aggregate measures of domestic activity were being dampened by a work stoppage at a major automobile company, now in its fourth week. The industrial production index increased slightly in September despite a decline in automobile output. Weekly retail trade reports indicated little change in nondurable goods sales from the advanced August-September level, although durable goods volume declined in reflection of the shortage of new cars. Employment in nonfarm establishments rose further in September, but the unemployment rate, at 5.2 per cent, was little changed

from August. Wholesale industrial prices remained broadly stable into early October, except for further marked increases in nonferrous metals prices.

Gross national product was estimated to have advanced at an annual rate of $9 billion in the third quarter, to a level 6.9 per cent above a year earlier in current dollars and 4.8 per cent higher in real terms. Consumption expenditures rose more than disposable income in the quarter, and business outlays for fixed capital continued to expand vigorously. On the other hand, residential construction expenditures declined somewhat, and businesses accumulated inventories at an estimated annual rate of only $1.7 billion, $2 billion below the second quarter's moderate rate.

Total bank credit increased substantially again in September, with the rise concentrated in the first half of the month. Both loans and investments declined in early October. Growth in the money supply in September, and in the third quarter as a whole, was at an annual rate of about 6 per cent—twice the rate prevailing in the first half of the year. According to preliminary indications the money supply rose substantially further in the first half of October.

Free reserves of member banks continued to average about $80 million in the 3 weeks ending October 7. In the following week, however, they rose to an estimated $186 million, chiefly because the level of float over the Columbus Day holiday weekend was substantially higher than expected.

In security markets, yields on 3-month Treasury bills increased several basis points further to 3.59 per cent. Long-term markets were characterized by a cautious tone, and yields on long-term Treasury securities edged up after late September. Yields on new issues of corporate bonds declined in recent weeks as the calendar of forthcoming offerings contracted, but even in this market investor caution was suggested by a build-up in dealer inventories of unsold bonds. It was reported that the Treasury soon would announce the terms of its November refunding,