

CRITERIA FOR FEDERAL RESERVE POLICY

I. Relation of this discussion to earlier discussions

Although various aspects overlap and cannot be separated neatly into compartments -

- A. The emphasis of the last discussion was on measures of the tone of the money market - that is, the degree of ease or tightness. This included discussion of such measures as:

Member bank reserve positions - total, required, excess, borrowed, and free reserves or net borrowings.
Interest rates, especially open market rates.

- B. The emphasis in this discussion will be on:

1. How the System can ascertain whether it should tighten, ease, or maintain the existing degree of pressure, and
2. Since this hinges on what it is trying to accomplish, what its ultimate objectives should be. I shall begin with ultimate objectives.

II. Some possible ultimate objectives

Introduction:

1. The yearning for precise objectives
 - a. Promotes clarity of thought
 - b. Imprecise objectives promote impressions that "anything can happen and everyone's idea is as good as anyone's."
 2. Hazards of precisely definite objectives in the real world
 - a. The more exclusive we become, the more we leave out that is relevant
 - b. The more inclusive we become, the more we include unlike things under one heading
- e.g. Money supply

A. Employment and unemployment

1. Is there some level or rate of unemployment that marks the boundary between inflationary and deflationary conditions?
2. How accurate is our measure of employment and unemployment?
3. How about hours of work?
64 million at 40 straight time hours not the same
(income-wise) as
32 million at 42 hours (with two hours at overtime) and
32 million at 38 hours
4. Wage rates, full employment, and inflation

B. Price stability

1. What measure should be used?
 - a. General wholesale index
 - b. Consumer index
 - c. Non-agricultural index
2. Problems of dispersion and weighting
If agricultural and industrial prices move in opposite directions and largely offset each other, should rise in the latter be disregarded to avoid additional pressure on the farmers?

Or should an attempt be made to restrain the rise in industrial prices partly to relieve the pressure on farmers from rising costs?

C. Growth - Whittlesey thesis at the A.E.A. meetings

1. How determine the appropriate rate of growth?
Is it constant over time?
2. The present - consumption vs. the future - investment
3. Growth in money supply
Is the rate of growth in the money supply an adequate guide to credit policy? Or, to phrase it another way, will the maintenance of a steady growth in the money supply at a rate equal to the long-term rate of growth of the economy assure achievement of the System's major objectives?

Should the System endeavor to promote changes in the money supply in keeping with the expansion or contraction of economic activity?

Or should account be taken of changes in the rate of turnover of the money supply, restraining the growth in the money supply in periods of rapid expansion in economic activity, and promoting more rapid growth in the money supply in periods of economic contraction?

- D. Relationship of credit policy to other major forces in the economy

Should the System undertake to counteract unstabilizing forces such as the following:

Inappropriate fiscal, debt management, or other Governmental policies?

Excessive labor demands in relation to productive efficiency?

Excessive business inventory accumulation or capital expenditures?

If so, should it try to oppose them directly, or keep its eyes fixed mainly on the over-all state of the economy in the effort to maintain general conditions conducive to restraint on errors or distortions in particular areas?

III. Short-run criteria

Introduction:

Ultimate objectives are inadequate guides to current operations. For example, if a stable price level had been our objective, we can say that it has been achieved over the last three or four years. BUT this period was marked by successive changes in credit policy:

1. Increasing tightness: 1952 - Summer 1953
(initially while wholesale prices were still falling in 1952)
2. Increasing ease: Summer 1953 to late 1954
3. Increasing tightness: late 1954 -

Neither the wholesale nor the consumer price index as such indicated the need for any of these changes in policy; but to the extent that monetary policy is influential, the changes were appropriate to maintenance of stable levels!

- A. Should we rely on the latest information or expectations? If the latter, on what should they be based?
- B. Should we rely on a few or on many measures of economic activity?
- C. Should we rely on a specified list or should we change the factors from time to time?