



# FEDERAL RESERVE BANK OF NEW YORK



## ANNUAL REPORT 1967



**FEDERAL RESERVE BANK OF NEW YORK**

February 28, 1968

To the Member Banks in the  
Second Federal Reserve District:

It is with great pleasure that I present our fifty-third Annual Report, reviewing the major economic and financial developments of 1967.

The past year was a trying one for the United States economy. A major inventory adjustment took place without serious consequences, and the economy moved on to new records of output, income, and employment. But the country was plagued by a number of economic ills. Delay in the application of fiscal restraint meant that the economic burden of the Vietnam war was reflected in a massive budget deficit, rising interest rates, mounting cost and price pressures, and a deterioration in the United States balance of payments. Violence in the cities pointed up the costs of poverty and discrimination to the country. The international financial system was rocked by the devaluation of sterling and the subsequent brief, but intense, stampede into gold. The threat to the dollar was countered as 1968 opened by the President's stringent new balance-of-payments program.

Monetary policy continued to ease through the first third of 1967 in order to prevent the downward tendencies in the economy from cumulating, and then remained essentially unchanged until late in the year. While the need to move toward a more restrictive policy became increasingly evident after midyear, uncertainty over the proposed tax surcharge, heavy Treasury financing, and pressure on sterling all made delay in changing the stance of monetary policy advisable. Toward the year-end, however, the setting changed and the System employed all the traditional instruments--the discount rate, open market operations, and reserve requirements--in moving toward somewhat firmer monetary conditions.

In 1968, economic policy must seek a reduction in inflationary pressures and a significant improvement in the balance of payments, both in the context of a growing economy. An appropriate mix of monetary and fiscal policies, including enactment of the long-needed tax increase, can make a major contribution to this effort.

A handwritten signature in cursive script that reads "Alfred Hayes".

ALFRED HAYES  
President

*Federal Reserve Bank  
of New York*

**FIFTY-THIRD  
ANNUAL REPORT**

*For the Year  
Ended on  
December 31, 1967*



*Second Federal Reserve District*



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*Fifty-third Annual Report  
Federal Reserve Bank of New York*

**1967: A Trying Year**

The United States economy avoided a recession in the first part of 1967 and moved on to reach new records of output, employment, and income. Yet, in the midst of unprecedented prosperity, the country was plagued by a variety of economic ills. The execution of economic policy was frustrated by lack of agreement on how the burden of the Vietnam war should be met. Delay in the application of fiscal restraint in the face of a large budget deficit and of inflationary pressures in the latter part of the year posed a serious dilemma for monetary policy; partly as a result, the policy of monetary ease was continued until late in the year, when the Federal Reserve System shifted its stance toward somewhat firmer credit conditions. Huge Treasury financing needs contributed to a surprisingly rapid rise in interest rates, in some instances to the highest levels in this century. An affluent nation was reminded of the extent of misery in our society by outbreaks of violence in many cities. A wage-price spiral gathered momentum during the year and threatened both domestic stability and the international standing of the dollar. The devaluation of sterling rocked the international financial system in November and led to a brief stampede into gold. The threat to the dollar, already plagued by a long succession of payments deficits, was countered as 1968 opened by the President's unprecedentedly stringent balance-of-payments program.

The problems experienced by the American economy in 1967 stemmed in large part from the cumulative strains of a military buildup superimposed since mid-1965 upon an almost fully employed economy. In the two and a half years following mid-1965, defense spending rose by 50 per cent. At the same time,

the United States attempted to continue meeting its responsibilities around the world and to its less fortunate citizens at home. Since all this was done without major fiscal restraint, it is perhaps less surprising that troubles ensued than that they were not greater.

The stresses that had developed in 1966, when appropriate fiscal restraint was not applied to moderate the boom, largely shaped the course of the domestic economy in 1967. In the first half of the year the economy had to adjust to the big overhang of inventories that had developed toward the end of 1966. Within two calendar quarters, inventory investment dropped from an annual rate of more than \$18 billion to practically nothing—the severest inventory investment adjustment on record. At the same time, plant and equipment spending edged off, following the upsurge of the preceding three years. And yet, under the stimulus of monetary and fiscal ease, the downturn in business outlays did not cumulate, confidence did not crumble, and the economy held steady. By midyear, the inventory adjustment was largely completed and the overall expansion quickened. In the fall, output was disrupted by major strikes in the automobile and other industries, but by November the economy was again moving strongly ahead. While defense expenditures showed signs of leveling off, business spending on both fixed capital and inventories was picking up pace and residential construction was extending the vigorous recovery that had started early in the year. The behavior of the consumer remained a puzzle. Throughout the year, consumer spending on goods and services grew fairly steadily, reflecting rising personal incomes. But the expected loosening of consumer purse strings did not occur, and individuals continued to save an unusually high proportion of their incomes. The Vietnam war was a major uncertainty depressing consumer spending, but no doubt anxiety over economic prospects, higher taxes, and rising prices also contributed.

The price situation in 1967 did indeed justify serious misgivings. In the first part of the year, the sluggishness in the overall economy was accompanied by reduced price pressures. Later, however, the advance in consumer prices accelerated and industrial prices started moving up once more. For 1967 as a whole, the broadest measure of price change, the GNP deflator, rose by 3 per cent over 1966, the largest annual increase in ten years. This occurred despite the fact that industrial capacity, continuing the rapid growth of earlier years, was not being fully utilized. The aftereffects of the excesses of 1966 persisted, as they do once inflationary tendencies develop. These tendencies became intensified in the last half of 1967, when the substantial completion of the inventory

adjustment gave impetus to the rapid advance of overall demands and inflationary expectations began to spread. Costs mounted steeply during the year as the growth of productivity slowed down and the advance in wages speeded up. Past and prospective increases in the cost of living, in particular, spurred labor demands for higher take-home pay.

The avoidance of inflationary wage settlements and price pressures is a major unresolved economic policy issue in a free society committed to steady growth and full employment. No industrialized democracy has yet found a way to resolve the problem, although a number have succeeded for limited periods and in special circumstances. Some observers have counseled direct controls or periodic recessions. Others regard inflation as a small and necessary price for absorbing into gainful and productive employment all those who, for reasons of racial discrimination or other hindrances, have not been able to find their rightful place in our society. But surely these diverse views all amount to a counsel of despair. The country has not brought into full play other measures that can achieve the same ends without the costs of inflation, recession, or controls. Greatly enlarged efforts by both government and business to train and place workers, along the lines of President Johnson's job opportunity program, deserve extremely high priority.

The Federal Reserve continued in 1967 to strive for the maintenance of an appropriate financial setting in which the overall goal of noninflationary growth could best be furthered. In the first half of the year, monetary policy worked hand in hand with fiscal policy to prevent the downward tendencies in the economy from cumulating. In the latter part of the year, the task of the System was made difficult by a variety of circumstances. The need to reduce the monetary stimulus and then actually to restrain the gathering demands in the economy became evident, but delay in changing the posture of monetary policy seemed advisable. In the first place, the outcome of President Johnson's recommendations for a program of fiscal restraint remained long in doubt. The heavy volume of Treasury borrowing, moreover, on a number of occasions argued against a shift in policy. At the same time, the escalation of interest rates and the great sensitivity that financial institutions carried over from 1966 threatened to magnify out of all proportion any System attempt to pull in the reins. Finally, the pound sterling, after a period of good recovery early in the year, was again in difficulty and an exacerbation of British problems had to be avoided.

Thus, the Federal Reserve, after having followed a policy of easing monetary conditions through the first four months of the year, maintained its policy of

ease until November. Then the devaluation of the British pound, the collapse of hopes of early enactment of a tax increase, a gap in the schedule of Treasury financing operations, and a steadying of the financial markets changed the setting for System policy. On November 19, the day after the British devaluation and a rise in the Bank of England's discount rate from 6½ per cent to 8 per cent, Federal Reserve Bank discount rates were raised to 4½ per cent from the 4 per cent level to which they had been lowered in April. Open market policy moved in December to achieve somewhat firmer monetary conditions and, just before the year-end, an increase in member bank reserve requirements against demand deposits was announced to take effect in January.

The behavior of financial markets throughout most of the year differed greatly from normal patterns during a period of monetary ease. Considerable financial stringency had developed in 1966 when monetary policy received little support from fiscal policy in the restraint of the boom. This stringency left its imprint on the behavior of lenders and borrowers throughout 1967. A new caution in the undertaking of financial commitments and a striving for liquidity thus dominated financial markets despite the turnaround of monetary policy. Long-term interest rates, which had turned down in the last months of 1966, reversed their course early in the spring and moved up rather steadily through the rest of the year. Corporate borrowers undertook a record volume of new long-term borrowing, as they strove to rebuild their liquid assets and to reduce their reliance on commercial banks. State and local governments also borrowed heavily, both for their own use and to finance corporate projects through issues of industrial revenue bonds. The bond markets digested the record volume of new offerings relatively well, notwithstanding fears in the second half of the year that exceptionally large Treasury financing needs would preempt much of the market supply of available funds. The System, when appropriate, used the need for reserve injections to help facilitate the market's functioning through purchases of coupon issues. The prospects of heavy Treasury borrowings after midyear also changed the course of shorter term interest rates. In response to monetary ease, these rates declined almost without interruption during the first four to five months of 1967, but in June they jumped sharply and continued to rise for the rest of the year.

Unlike the markets for securities, commercial banks and thrift institutions experienced a year relatively free from strains. Interest rate relationships, at least during the first part of the year, were more favorable to the savings institutions than in 1966. Given a high general level of consumer saving, flows of funds into

these institutions were thus substantial during most of the period. As a result, mortgage lending, particularly by the savings and loan associations, rose briskly from the depressed level of 1966. The commercial banks were also able to increase their time deposits sharply and, as the Federal Reserve supplied a growing volume of bank reserves, total commercial bank credit expanded very rapidly. In fact, the commercial banks in 1967 almost doubled their share in the total credit extension in the economy from the low of 1966, and raised it considerably above the average of earlier years. With private demand for bank loans relatively moderate and Government financing very heavy, more than one half of the year's record bank credit expansion was in the form of increased holdings of United States Government and municipal securities. In the closing months of the year the pattern of financial flows began to change. As interest rate differentials turned increasingly against the commercial banks and the thrift institutions and in favor of market instruments, inflows of savings to the financial intermediaries slackened. At the same time, the rapid growth of bank credit and of the money supply slowed.

In 1967, as in earlier years, considerations of the United States balance of payments played a role in the Federal Reserve's conduct of monetary policy. But with high and rising interest rates already moderating capital outflows, the scope for additional direct monetary influence on the payments deficit was quite limited. As it turned out, the liquidity deficit deteriorated sharply during the year and reached \$3.6 billion for 1967 as a whole, as against \$1.4 billion in 1966. The trade surplus failed to improve, as a slowdown in the economies of our major trading partners limited the rise in our exports. At the same time, military expenditures abroad jumped further—the balance-of-payments costs of the Vietnam war were estimated at \$1½ billion annually—and capital outflows increased. The troublesome United States balance-of-payments position made the United States dollar especially vulnerable in the closing weeks of 1967, when the world's monetary system felt the shock of sterling devaluation.

The measures that had been instituted by the British government since 1964 to restore Britain's international payments position, particularly the tough program that followed the mid-1966 sterling crisis, had by the start of 1967 finally shown signs of bearing fruit. Britain's basic payments position moved into surplus, volatile capital flows turned in London's favor, and Britain was able to liquidate all the short-term debts it had outstanding to the Federal Reserve and other central banks while adding substantially to its reserves. But then came a quick succession of adverse developments, including in particular the Arab-

Israeli war in June and its wide repercussions. The British payments position weakened once more, capital started moving out, and confidence in sterling sank to another low. In November, the British government faced the choice of imposing still further unpopular restraints on the British public to restore equilibrium at the existing sterling parity, which was coming under increasing domestic criticism, or of devaluing the British currency and backing up devaluation with very similar domestic restraints. It chose the latter course. This decision, once taken, was accepted without countermeasures by most of the rest of the world. Indeed, leading industrial nations continued to provide support in the form of new credits which would also have been available had Britain opted to stay with the old parity.

The change in sterling parity inevitably led to turmoil in international financial markets. In the uncertainty that was created, other currencies—and particularly the dollar—became suspect, and an unprecedented wave of speculation buffeted the gold markets. In the face of this threat to the world monetary system, central banks once again moved promptly to meet the challenge. The United States and the other participants in the Gold Pool reaffirmed their support of the fixed monetary price of \$35 per ounce of gold and made massive sales of gold in the London market to hold the market price steady. Measures were also taken to discourage private purchases of gold, to ease strains in the Euro-dollar market, and to calm forward exchange markets. In addition, most of the Federal Reserve swap arrangements were substantially enlarged, raising the total of the swap facilities in the network to over \$7 billion. Earlier in the year, international financial cooperation had passed another important milestone when the board of governors of the International Monetary Fund approved the outline of a plan to establish special drawing rights in the IMF to supplement existing international reserve assets in case of need.

Cooperative measures among the monetary authorities of the leading countries and the development of new financial mechanisms, however, are not sufficient to ensure the smooth functioning of the world payments system. Policies to adjust the payments balances of individual countries in order to avoid extreme deficits and surpluses are vital. The Vietnam war had interrupted United States progress to a balanced payments position. The devaluation of sterling had exposed the United States dollar and thus the entire world financial system to renewed questioning. In this setting, President Johnson acted at the turn of the year to reduce the country's payments deficit through a series of drastic measures. To the extent that these measures put further obstacles to the flow of

international transactions, they are of course undesirable in the long run. But they are to be regarded as a means of buying the time that is needed in order to restore payments balance through the working of market forces within the framework of appropriate policies. They are, moreover, greatly preferable to the chaotic conditions that could arise from failure to defend the dollar.

As 1968 opened, it was clear that restoration of fiscal order was priority number one for United States economic policy. Fiscal restraint was called for to reduce a large budget deficit, to moderate an accelerating domestic expansion, to curb the rise in costs and prices, and to help restore payments equilibrium. Beyond this, however, the American nation faces basic decisions about longer run priorities. The United States has taken on a great many responsibilities around the world, and at the same time it faces massive economic and social problems at home. The country's productive resources are enormous, but we have not yet harnessed our strength properly. If we do not, the troubles of 1967 will seem very minor indeed.

## THE UNITED STATES ECONOMY

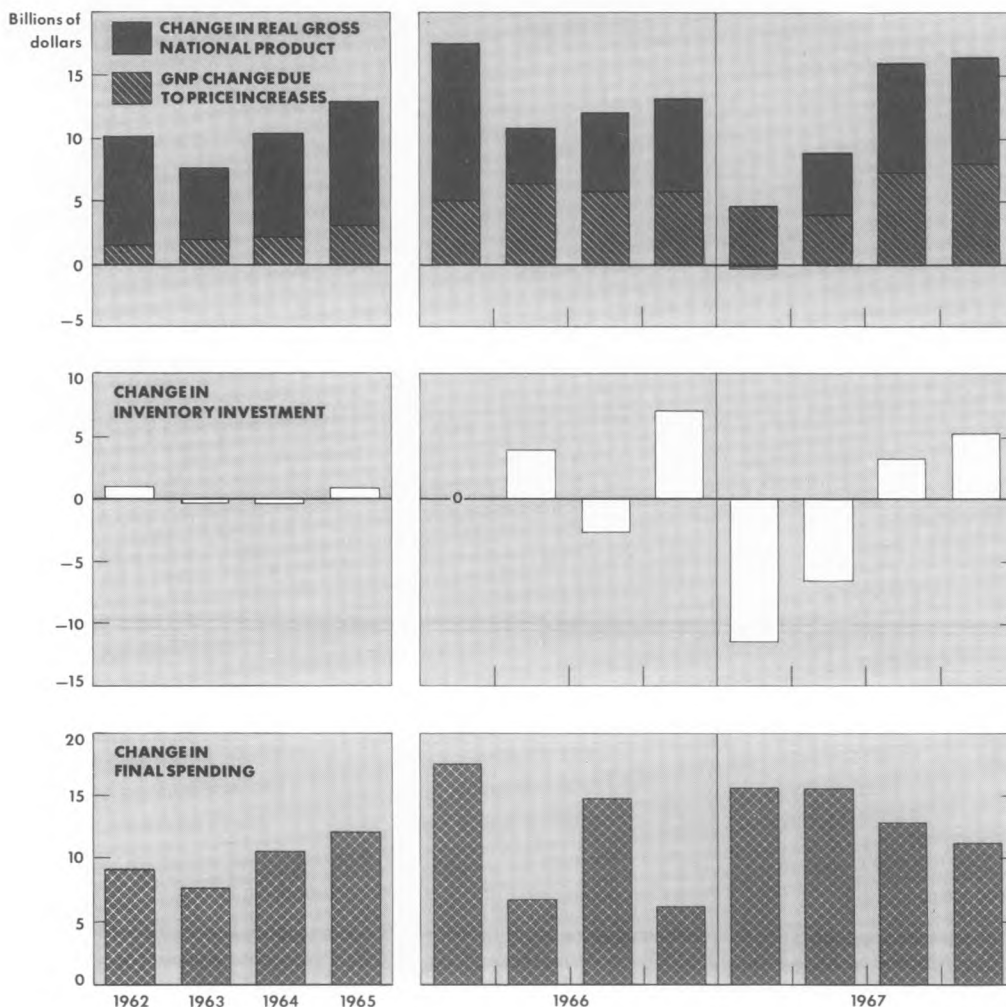
### **Business Conditions: Readjustment and Renewed Growth**

The pattern of economic activity was uneven during 1967. In the first part of the year the growth of the economy was dampened by a massive inventory adjustment. However, final spending—gross national product (GNP) minus inventory investment—held up very well during this period as government expenditures advanced sharply and residential construction turned up. Around mid-year the tempo of business activity began to quicken: inventory accumulation started to increase again and residential construction spending accelerated. Business fixed capital spending also strengthened in the latter part of the year. Thus, the economy posted a strong gain during the second half of 1967 despite a wave of major strikes. Over the year as a whole, GNP advanced to a record \$785 billion—an increase of \$42 billion over the total value of goods and services produced in 1966—and carried the current economic expansion through its seventh consecutive year, the longest advance in United States history.

Although the moderate pace of economic growth in the first part of the year temporarily weakened the pressure of demand on prices, the cost environment was more conducive to inflation in 1967 than it had been in the previous years of the current decade. Productivity grew very slowly during the year, but wage increases accelerated. As a result, unit labor costs advanced sharply. Under these circumstances, the demand pressures that began to develop at the end of the second quarter were quickly reflected in price increases, and these in turn contributed to intensified wage demands. For the year as a whole, over half of the increase in GNP represented price increases (see Chart 1).

**INVENTORY ACCUMULATION DECLINES SHARPLY, BUT FINAL SPENDING REMAINS STRONG.** The weakness in aggregate demand in the first half of 1967 reflected an exceptionally large cutback in inventory spending. In 1966, stocks had accumulated at a rapid rate, and by the fourth quarter of that year inventory spending had reached an annual pace of over \$18 billion. The buildup

**Chart 1. CHANGES IN GROSS NATIONAL PRODUCT AND SELECTED COMPONENTS:** The advance in GNP in the first and second quarters of 1967 was slowed by a large decline in the rate of inventory accumulation. During the same period, however, a sharp increase in government outlays and a turnaround in residential construction expenditures contributed to substantial growth in final spending. GNP increased much more rapidly in the second half of the year, as inventory accumulation advanced and final demand continued to rise quite rapidly.



Data for 1966-67 are quarterly changes in seasonally adjusted annual rate levels. For 1962-65, data are year-over-year changes divided by 4 for comparability.

in inventories was most rapid in the durables manufacturing sector, particularly in the defense and capital goods industries. The substantial rise in the goods-in-process component of manufacturers' stocks indicated that some of the buildup was intentional and reflected the acceleration of capital and defense spending. However, the sizable increases in stocks of finished goods in both the manufacturing and trade sectors pushed inventory-sales ratios to their highest levels in several years, suggesting that a disturbingly large part of the inventory accumulation was the result of unexpectedly small gains in sales. Thus, the stage was set for the slowdown in inventory spending that occurred in 1967.

In an effort to bring inventories into better alignment with sales, businessmen reduced the annual pace of inventory accumulation by \$18 billion in the first half of 1967, the largest cutback in inventory spending in the postwar period. Retailers let their inventory holdings actually decline over the first seven months of the year and were particularly successful in reducing their stock-sales ratio. Inventory cutbacks at the retail level meant slower sales in the wholesale sector, where the downward adjustment of stocks was accordingly more gradual. By midyear, however, the inventory-sales ratio in the trade sector as a whole had declined to its relatively low 1965 level. The problem of excessive inventories was much more serious in manufacturing than in the trade sector. Although manufacturers added relatively small amounts to their inventories in the first half of the year and actually cut back their stocks in June, inventory-sales ratios—particularly for durables manufacturers—remained high until late in the year, when sales advanced sharply.

This massive readjustment of inventory spending removed the overhang of unwanted stocks in most sectors, however, and in the second half of the year sales picked up, expectations became more buoyant, and inventory accumulation accelerated. During this period, businessmen added to their stocks at an annual rate of \$6½ billion, and this turnaround in inventory accumulation, along with the continued strength of final demand, was a major factor contributing to the vigorous growth of the economy in the second half of the year.

Although the sharp decline in inventory accumulation during the first half of 1967 constituted a major drag on economic activity, other spending held up remarkably well and was a source of considerable strength throughout the year. The advance in final demand in the first quarter of 1967 was well over twice the increase during the final quarter of 1966 and was largely attributable to an accelerated rate of expansion in government outlays. Government spending at both the Federal and the state and local levels advanced very sharply in the first

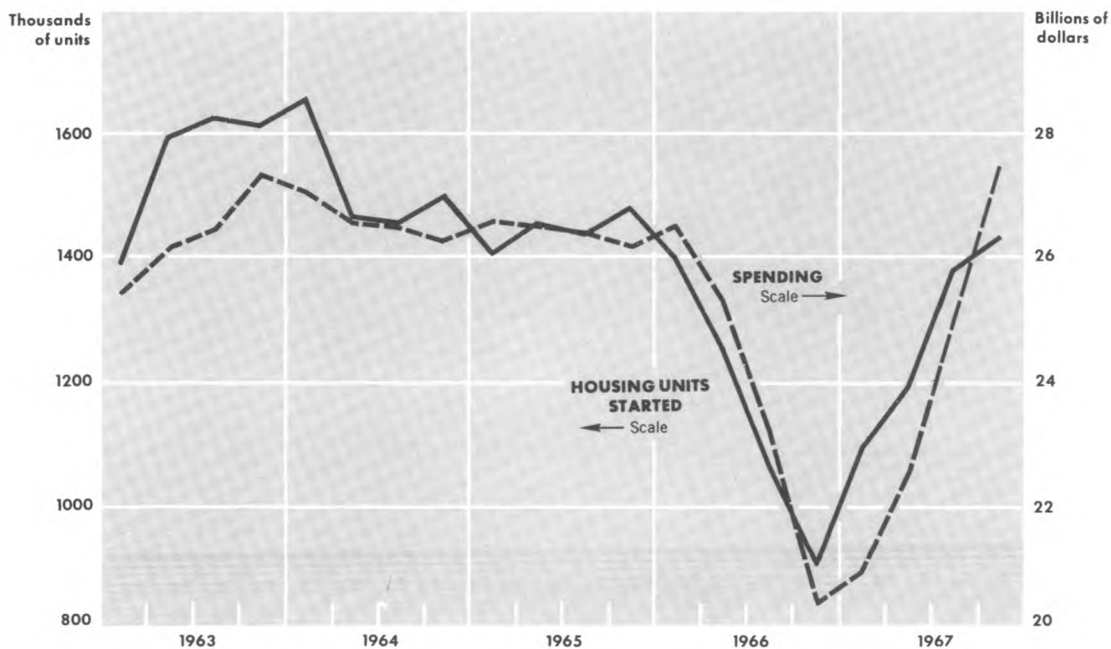
quarter, and for 1967 as a whole the increase in total government purchases of goods and services accounted for over half of the rise in GNP, the highest proportion since 1958.

The growth in Federal spending tapered off during the last three quarters of 1967 despite a large retroactive pay increase for both military and civilian government employees late in the year. Defense spending grew less rapidly as the year progressed but continued to play a dominant role in the Federal sector and to exert an important influence on economic activity in general, as it has since the escalation of the Vietnam conflict in mid-1965. Defense expenditures rose 20 per cent in 1967, with a particularly large increase occurring in the first quarter. Federal nondefense outlays for goods and services advanced by almost 5 per cent last year, in contrast to a slight decline in 1966 when funds for highways and other public projects were impounded to help ease inflationary pressures. State and local government spending continued to rise steadily to a total of \$86½ billion in 1967, an advance of 12 per cent over the previous year.

**THE RESURGENCE OF RESIDENTIAL CONSTRUCTION.** Private spending was strengthened by a rebound in residential construction in 1967. Home building was severely depressed in 1966, as heavy demands for credit in conjunction with monetary restraint forced market rates of interest to the highest levels in decades. Mutual savings banks and savings and loan associations, which are traditionally the largest sources of home mortgage credit, were unable to compete successfully for savings and had to restrict the supply of funds to the mortgage market. Builders and potential homeowners were often unable to obtain credit and had to defer the construction and purchase of housing until such credit could be obtained. Late in 1966, savings flows into thrift institutions began to accelerate, as market yields declined in response to the move toward a less restrictive monetary policy and as the rate of personal saving increased. Rising inflows enabled these institutions to expand their mortgage loans and commitments.

The recovery in residential construction quickly followed the easing of financial conditions toward the end of 1966. The upswing gained momentum in the spring and continued almost uninterrupted throughout 1967. The rising trend of household formation and the backlog of demand that was deferred in 1966, in addition to the improved supply of credit, helped to spur the recovery. Private nonfarm housing starts advanced during most of the year (see Chart 2) and, in the fourth quarter of 1967, averaged over 1.4 million units at an annual rate,

**Chart 2. RESIDENTIAL CONSTRUCTION: After falling sharply in 1966, largely in response to the credit squeeze, private nonfarm housing starts advanced strongly in 1967 as credit market conditions eased. Spending on residential construction also recorded a substantial gain over the course of the year. Indeed, by the fourth quarter of 1967, current dollar outlays had reached the highest annual rate in four years.**



Quarterly data are expressed at seasonally adjusted annual rates.

the highest average since the October-December period of 1965 and sharply higher than the average of less than 900,000 units in the fourth quarter of 1966. Spending on residential construction rose markedly from the fourth quarter of 1966 to the fourth quarter of 1967 and, in the latter period, reached an annual rate of \$27½ billion. At the close of the year, however, fears of another squeeze on the mortgage market and the home-building industry began to arise, as market yields on many instruments surpassed their 1966 peaks, threatening to divert the flow of savings away from financial intermediaries into the open market.

**BUSINESS FIXED INVESTMENT.** Business fixed investment outlays leveled off in 1967, in marked contrast to the three previous years in which capital spending contributed substantially to the economy's growth. After reaching an annual rate of almost \$83 billion in the last quarter of 1966, business fixed investment spending declined modestly through much of 1967. The slackening in the investment boom reflected the general slowdown in economic activity in the first half of the year, when inventories were excessive, sales were sluggish, and there was an easing in capacity pressures. The high cost and limited availability of credit in 1966 and the suspension of the 7 per cent tax credit and accelerated depreciation schedules in October of that year also served to dampen capital spending in the early part of 1967. Moreover, rising labor and materials costs, along with slow productivity growth and lagging demand, put a squeeze on profits, which further slowed business spending on new production facilities. In June, however, the tax credit and accelerated depreciation schedules were reinstated and, in the third quarter, corporate profits advanced for the first time in a year. These developments, plus a noticeable strengthening of the business outlook, contributed to an upturn in capital spending in the latter part of the year, despite uncertainty over the outcome of Congressional debate on the proposed surcharge on corporate and individual income taxes. For the year as a whole, business fixed investment spending was only about 3 per cent greater than in 1966, compared with an average annual growth of 14 per cent in the three previous years. While most of the 1967 advance represented price increases, the high level of capital spending in current dollar terms contributed to heavy corporate borrowing in the bond markets throughout the year.

**CONSUMERS EXERCISE CAUTION.** Consumer spending advanced only moderately in 1967 despite a continued strong advance in disposable personal income. Consumers were cautious in view of uncertainties stemming from the Vietnam war and the possibility of a tax increase. Rising prices and strikes also had a dampening effect on consumer spending. For 1967 as a whole, consumer expenditures rose by only 5½ per cent. The increase in spending on durable goods was the weakest since 1961, and consumer outlays for nondurables grew less rapidly than in the previous three years. In contrast, spending on services continued to advance at a rapid rate. However, a large share of the increase in consumer outlays for services, as well as for both durable and nondurable goods, merely reflected higher prices.

Personal saving rose by an exceptionally large 30 per cent in 1967 as a result of consumers' reluctance to increase spending in line with the continued sharp rise in disposable income. Although the advance in wage and salary income moderated as the growth of the economy slowed in the first half of the year, Government transfer payments, such as welfare benefits, relief, and unemployment compensation, took up some of the slack and, after midyear, the increase in wage and salary income accelerated along with the quickening tempo of business activity. The decision of consumers to save, rather than spend, an unusually large fraction of this income resulted in a sharp rise in the savings rate—the ratio of personal saving to disposable personal income—which soared to over 7 per cent last year, compared with an average of just over 5½ per cent in the previous years of the current expansion. The relatively high interest rates that prevailed through most of 1967, in addition to rising incomes and consumer cautiousness, may well have provided an inducement to higher saving during the year.

**COST AND PRICE INCREASES ACCELERATE.** Although the economy continued to utilize its labor resources at a relatively high rate in 1967, pressures on its physical productive facilities eased. The capacity utilization rate in manufacturing declined to an average of just over 85 per cent, the lowest rate in three years and considerably below the preferred rate. The drop was particularly sharp in the first half of the year, when industrial production declined in response to the inventory adjustment while new plant and equipment were becoming available at a fairly rapid rate as a result of the large increase in investment expenditures in recent years. Although the drop in capacity utilization was widespread, the rate remained high in a few industries, such as aerospace, rubber, and petroleum refining. Moreover, with aggregate demand increasing sharply in the second half of the year, the overall capacity utilization rate edged upward in the fourth quarter, despite the fact that production was crippled by strikes in the auto, copper, steel-hauling, and farm equipment industries.

Conditions remained tight in the nation's labor markets in 1967, and the overall unemployment rate averaged 3.8 per cent, unchanged from the 1966 average. The civilian labor force declined somewhat over the first five months of the year but then increased sharply, and the growth in the number of employed persons kept pace. The average rate of unemployment of married men remained below the 2 per cent level in 1967, but the expanding number of teen-

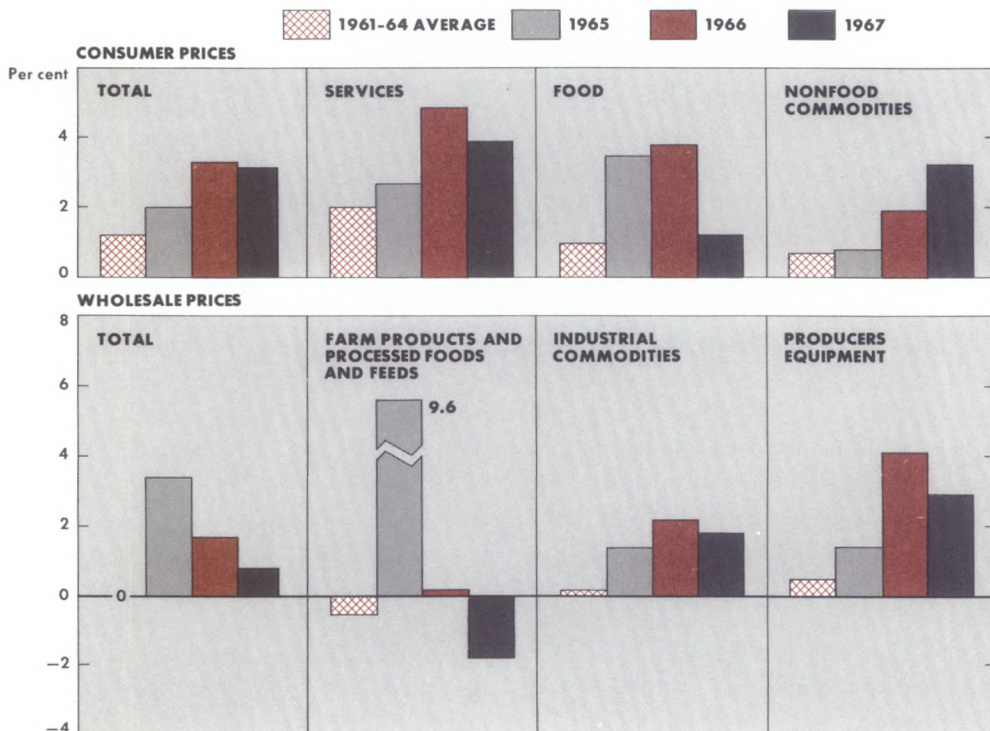
agers and nonwhites who could not find employment was a reminder of the urgency of job training and other programs necessary for equipping these workers with the skills required by an increasingly complex economy.

Wages and fringe benefits increased faster in 1967 than in any other year of the current expansion, reflecting in part the shortage of skilled labor and the generally tight conditions in the labor market. Moreover, the rapid growth of corporate profits in recent years and the desire to recoup purchasing power lost through rising prices in 1966 induced unions to demand large wage and benefit increases. Thus, the median annual increase in negotiated wage and fringe benefits was over 5½ per cent in 1967, compared with just over 4½ per cent in 1966 and considerably smaller increases in earlier years. While wages increased rapidly during the year, productivity growth was minimal—largely as a result of the dampening effects on production of the inventory overhang in the first part of the year and major strikes in the latter part—and cost pressures mounted. In manufacturing, output per man-hour rose less than 2 per cent from December 1966 to December 1967, while labor costs per man-hour advanced more than 5½ per cent. Moreover, toward the year-end, auto industry settlements, which set the pace for many other industries, threatened to establish a pattern of wage and benefit increases of over 6 per cent, and it appeared that cost pressures would continue to be severe in 1968.

With such large cost increases in 1967, producers had to accept lower profits or try to pass the rising costs on to their customers in the form of price increases. In the first half of the year, when aggregate demand was sluggish, producers found it difficult to raise prices. Thus, profits declined and prices rose only modestly. As demand began to increase sharply around midyear, however, prices increased on a broad front and profits edged upward.

Consumer prices rose throughout 1967, and by the year-end they were 3 per cent above the level at the end of 1966 (see Chart 3). A decline in food prices exerted a moderating influence on the advance in the overall level of consumer prices during the first third of the year, but then a sharp upturn in food prices during the summer months contributed to the accelerating rise in the overall index. Prices of nonfood commodities and services advanced very rapidly beginning in late summer and, although food prices declined again in the fall, the general level of consumer prices continued to rise. Wholesale prices were more stable over the course of the year—rising by less than 1 per cent from December 1966 to December 1967—as agricultural and industrial prices moved in opposite directions during most of the year. Industrial prices were

**Chart 3. RISING CONSUMER AND WHOLESALE PRICES:** Consumer prices rose rapidly in 1967 despite a very modest rise in food prices. The increase in prices of nonfood commodities was markedly above advances in recent years, and service prices continued to move sharply upward. Wholesale prices rose less rapidly in 1967 than in the previous two years, as agricultural prices dropped sharply. However, increases in prices of industrial commodities and producers equipment were substantial in the second half of 1967, reflecting both cost and demand pressures.



Data are percentage changes on a December-to-December basis.

unchanged from February to August but rose rapidly in the last five months of the year, reflecting rising costs in manufacturing and the pull of accelerating demand.

## **Monetary Policy and Credit Markets: Uncertainties and the Quest for Liquidity**

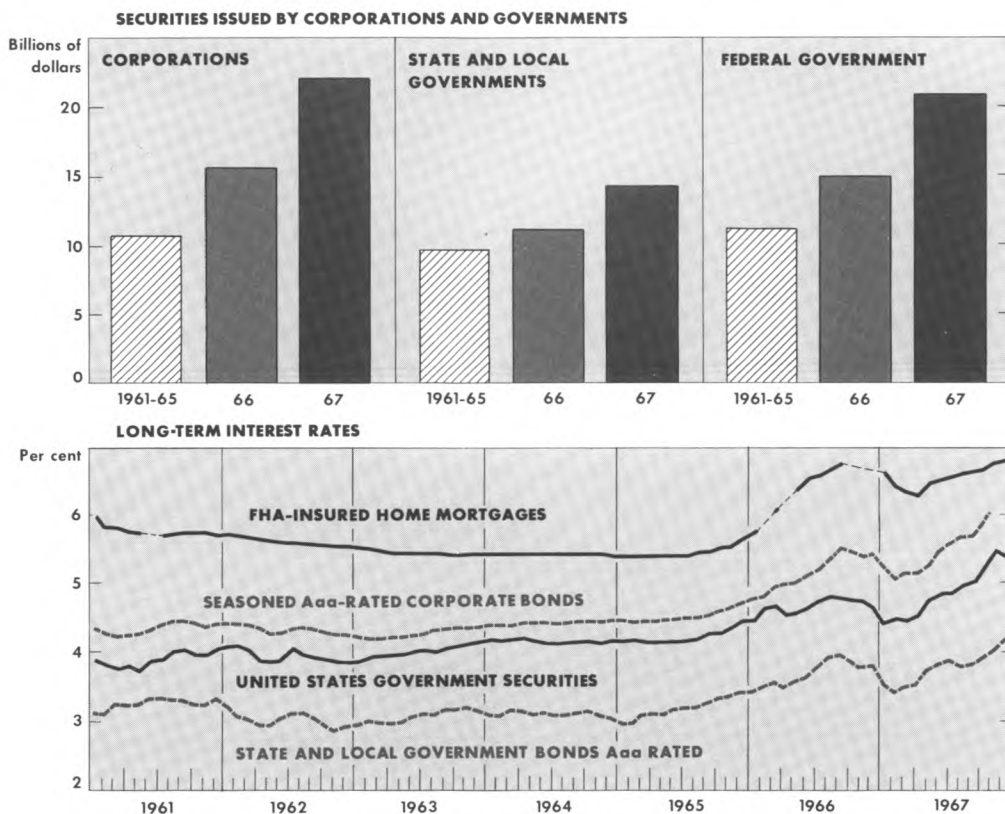
Monetary policy was faced with a complex task in 1967. It sought, in an atmosphere clouded by uncertainties, both to promote orderly economic growth and to restrain inflationary pressures. At the same time, policy had to take into account the pronounced rise in the demand for liquidity by all sectors of the economy in the wake of the 1966 liquidity squeeze. The widening balance-of-payments deficit and recurrent international financial tensions also played key roles in policy decisions. Moreover, the implementation of monetary policy was complicated by the size and timing of the Treasury's financing operations.

In order to facilitate the readjustments that were occurring in the economy and to accommodate the increased demand for liquidity, the Federal Reserve in the early part of 1967 continued the move toward an easier monetary policy which had been initiated late in 1966. After easing gradually through the first third of 1967, monetary policy remained essentially unchanged until late in the year. During the first part of 1967, financial conditions were relatively easy and yields on money market instruments and long-term bonds dropped quite sharply in response to the shift in monetary policy (see Charts 4 and 5). However, the fall in interest rates was short-lived, as record borrowing in the bond markets forced interest rates upward, and by the year-end many longer term yields had reached the highest levels in decades.

While rising interest rates undoubtedly had some restraining effect on the economy, the rapid advance in bank credit and deposits caused increasing concern as inflationary pressures mounted in the second half of the year. Nevertheless, caution in instituting a less easy monetary policy seemed advisable. The Administration's fiscal restraint program was still under consideration, and the pound was subject to difficulties in the exchange markets. Moreover, the Treasury's financing operations often argued against a change in policy. Toward the year-end, these obstacles to a change in policy were removed: it became clear that a tax increase would not be enacted in 1967, and sterling was devalued. All three traditional instruments of monetary policy were then used to move toward restraint. The discount rate was increased in the latter part of November; in December, open market policy firmed and the Board of Governors of the Federal Reserve System announced an increase in reserve requirements to become effective in January 1968.

**RIISING PRESSURES IN THE CAPITAL MARKETS.** The capital markets were subjected to unprecedented demands in 1967, and expectations of stringent

**Chart 4. CAPITAL MARKETS AND LONG-TERM INTEREST RATES:** Corporations and state and local governments borrowed record amounts in the bond markets in 1967, and the Federal Government borrowed more in the market than it had since World War II. Long-term rates were edging downward as the year opened, but by the year-end the heavy demands for funds pushed most rates to the highest levels in many decades.



Federal Government securities issues include participation certificates sold to the public. Data for securities issued during 1961-65 are annual averages. Mortgage interest rate data are the average yields in secondary markets for Federal Housing Administration-insured mortgages on new homes with thirty-year maturity. For short periods following changes in the maximum contractual rate, secondary market yield data are not available; such periods are indicated by broken lines.

market conditions and rising interest rates persisted through much of the year. Borrowing by corporations and state and local governments reached record levels in 1967, and the Treasury entered the market on a major scale in the second half. Thus, despite the accommodative monetary policy pursued by the Federal Reserve System, interest rates moved sharply higher.

In the first half of the year, funds generated internally by corporations declined rather sharply, and corporate liquidity was further strained by heavy accelerated tax payments to the Treasury. Corporations found it necessary to rely very heavily on external sources of financing, and in the first six months of 1967 a record \$10½ billion was raised through the issuance of long-term bonds. Much of the proceeds was used to clear lines of credit at commercial banks and to finance a continued high level of capital spending. In the second half, the volume of financing exceeded \$11 billion, reflecting accelerated inventory spending, anticipations of more stringent market conditions, and continued efforts to replenish liquidity. Long-term interest rates on corporate securities, which had begun to ease late in the summer of 1966, declined until the middle of the first quarter. However, by midyear, seasoned Aaa bond yields had risen more than 50 basis points above the 1967 low and were above the 1966 peak. By the year-end, yields had increased by almost another 70 basis points.

Similarly, offerings of state and local governments increased dramatically in 1967, as their outlays on schools, roads, utility operations, and other projects continued to rise. The issuance of industrial revenue bonds was heavy—perhaps in anticipation of possible changes in the tax-exempt status of these obligations. Total borrowing in 1967 rose to over \$14 billion, by far the heaviest volume of bond financing on record. Yields on tax-exempt issues fell sharply in the early part of 1967, paralleling yield movements in other bond markets but, by the year-end, yields had climbed about 80 basis points above earlier lows despite record purchases of tax-exempt securities by commercial banks.

The first half of the calendar year is normally marked by debt redemption by the Treasury, and the January-June period of 1967 was no exception. In the second half, however, the financing needs of the Federal Government (including Federal agencies) were very heavy, and gross cash borrowing from the public for the year as a whole exceeded \$20 billion, compared with \$15 billion in 1966. While most of these issues were in short maturities, the impact on the cost and availability of funds in all markets was extensive. Yields on long-term Government bonds declined about 25 basis points in January 1967 and then rose quite steadily until December when they eased slightly. At the year-end, yields on

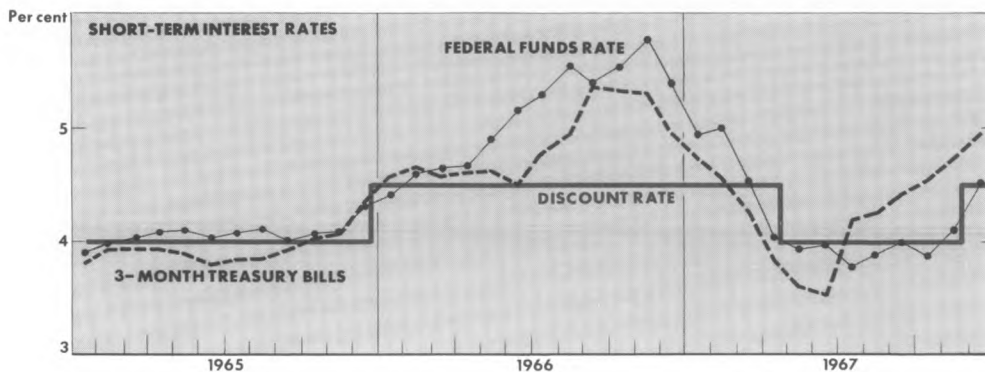
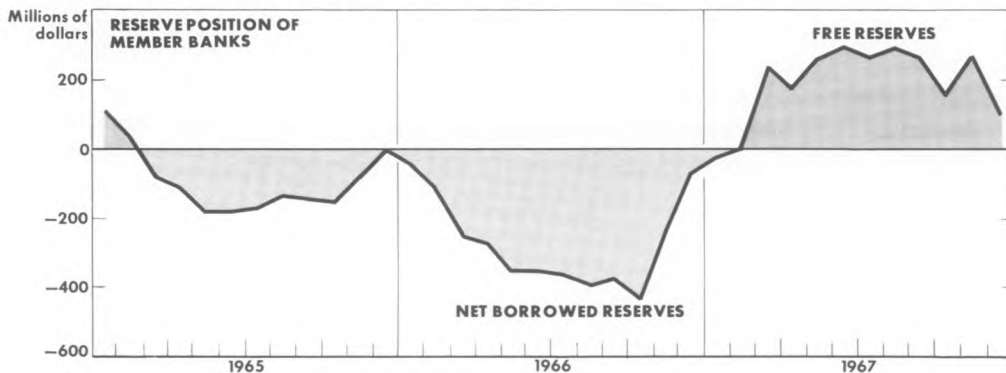
these issues were almost a full percentage point higher than January levels.

**MONETARY POLICY AND THE MONEY MARKET.** During the opening months of 1967, monetary policy continued the move toward ease—initiated late in 1966—to lessen the impact of the inventory adjustment then in progress and to meet the pressing demand for liquidity throughout the economy. In this respect, policy was particularly concerned with fostering market conditions conducive to large and growing flows of funds into the thrift institutions, since their liquidity was crucial in sustaining the rebound in residential construction that was getting under way. Thus, ample reserves were made available to the banking system, and member banks' free reserves (excess reserves minus borrowings at Federal Reserve Banks) rose from a daily average of minus \$431 million in October 1966 to minus \$16 million in January 1967. By March, free reserves had become positive for the first time in two years and from then on generally ranged between \$250 million and \$300 million until December. Daily average member bank borrowings from the Federal Reserve fell from a September 1966 peak of \$766 million to about \$100 million in May 1967, and they remained near that level until late in the year. Short-term market rates of interest generally declined promptly in response to greater reserve availability.

While the shift to an easier monetary policy was largely accomplished through open market operations, two other measures were taken during early 1967 in implementing this policy. On February 28 the Board of Governors of the Federal Reserve System announced a reduction in reserve requirements against all savings deposits and the first \$5 million of time deposits at each member bank. The required reserve ratio on such deposits was lowered from 4 per cent to 3 per cent in two stages during March, and approximately \$850 million in reserves was freed. Then, on April 6, the board of directors of this Bank, as well as those of nine other Federal Reserve Banks, voted discount rate reductions of  $\frac{1}{2}$  percentage point, subject to review and determination of the Board of Governors, and shortly after the directors of the two remaining Federal Reserve Banks voted similar reductions. The Board of Governors approved these actions, and they were immediately followed by large downward rate adjustments on short-term money market instruments. By midyear most rates had reached their low point for the year.

Thereafter, pressures in the capital market began to spill over into the money market, and short-term yields began to rise again. Expectations of extremely

**Chart 5. FREE RESERVES AND SHORT-TERM INTEREST RATES: Under the stimulus of more generous reserve availability, short-term interest rates eased during the first half of 1967. However, mounting pressures in all sectors of the credit market began to pull these rates upward around midyear, although free reserves remained relatively high until December when the shift toward less ease in monetary policy began to take effect.**



All data except the discount rate are monthly averages of daily figures.

heavy Treasury demands on the market contributed to the turnaround in short-term rates. With yields still above the 4¼ per cent ceiling on coupon rates for Government bonds, the Treasury was forced to borrow substantial amounts of funds in the short- and intermediate-term securities markets. Heavy Federal Government financing in the second half of the year thus tended to drive up short-term

rates, and expectations of further rises stimulated the upward movement.

Despite mounting cost and price pressures and a persistent deterioration in the balance of payments, the Federal Reserve continued to supply reserves liberally until late in the year. During the spring and early summer this policy helped to restore the liquidity absorbed from the economy in 1965 and 1966, but after midsummer the continued rapid growth of bank credit and deposits became an increasing cause for concern. However, the System was also apprehensive that market rates of interest might rise so high that the flow of savings would be diverted from financial intermediaries and toward open market instruments, choking off the supply of mortgage money. At the same time, a shift to a more restrictive monetary policy after midyear was made difficult by the need to facilitate the Treasury's very heavy financing program for the second half of the year. The System also sought to avoid any action that might hinder the passage of the proposed tax surcharge. Moreover, care had to be taken to avoid adding to existing pressures on the already weak pound.

On November 18 the British devalued the pound and increased their bank rate from 6½ per cent to 8 per cent. In view of these developments, a special meeting of this Bank's board of directors was held on Sunday, November 19, at which the directors considered the effects of these actions on the international position of the dollar, and they reviewed domestic economic and financial conditions. On the basis of their review, the directors concluded that decisive action was necessary to safeguard the position of the dollar and that in the circumstances it would be appropriate to increase the discount rate of this Bank from 4 per cent to 5 per cent, subject to review and determination of the Board of Governors. However, the Board of Governors did not approve the 5 per cent rate established by the Bank's directors. The directors then reviewed their action and that of the Board of Governors; after extended discussion and consideration, the directors unanimously reaffirmed their judgment that a discount rate increase of 1 percentage point would be appropriate in the circumstances. However, in the light of the Board's action, the directors reluctantly voted to establish the discount rate at 4½ per cent, effective the following day. The Board of Governors approved this action, as well as similar discount rate increases by nine other Federal Reserve Banks (the two remaining Reserve Banks soon took the same action). In announcing the discount rate increase on November 19, the Board of Governors noted that the System "had taken actions to assure the continued orderly functioning of United States financial markets and to maintain the availability of reserves to the banking system on terms and conditions that will

foster sustainable economic growth at home and a sound international position for the dollar”.

The System was, of course, concerned with the possible impact of the weekend's developments on the domestic securities markets and took timely action to forestall the emergence of disorderly market conditions and to smooth the adjustment to a viable new price structure. With these objectives in mind, the Manager of the System Open Market Account and other officers of this Bank's Open Market and Treasury Issues function met late Sunday afternoon, November 19, and worked out detailed plans for operations in the Government securities market the next day. Thus, before the usual opening of the market on Monday morning, the System took the initiative by bidding for relatively large amounts of coupon issues in all maturity ranges, with a view to removing most of the overhang of securities remaining from the recent Treasury financing. This decisive action headed off potential liquidation by dealers in an unreceptive market and facilitated an orderly decline in prices. The action was followed by the purchase of a substantial volume of Treasury bills to assist the short-term market in adjusting to the weekend's developments. The System's prompt and firm action early Monday morning was a primary factor in the orderly transition to lower Government securities prices. Money market rates and the prime rate charged by commercial banks moved up quickly after the discount rate increase.

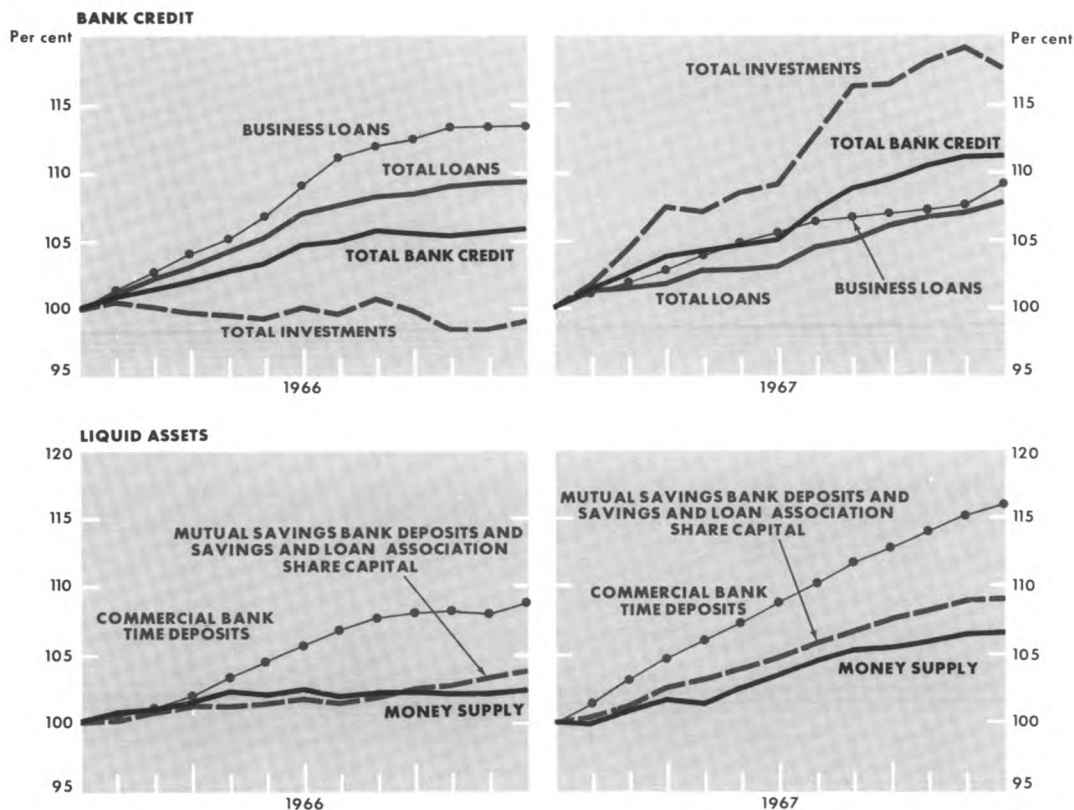
The System followed up the discount rate increase with a shift to a firmer open market policy in mid-December, and late in the month the Board of Governors announced an increase in reserve requirements against demand deposits in excess of \$5 million at each member bank, to take effect in January 1968. The reserve ratio was raised from 16½ per cent to 17 per cent at reserve city banks and from 12 per cent to 12½ per cent at other member banks. This measure increased required reserves by about \$550 million and clearly confirmed the System's intention to reduce reserve availability.

**ACCELERATED GROWTH OF BANK CREDIT, MONEY SUPPLY, AND OTHER LIQUID ASSETS.** The provision of ample reserves to the banking system facilitated the rapid growth of bank credit in 1967 (see Chart 6). The desire of commercial banks to increase their liquidity in 1967 was partly evidenced by the composition of this growth, which provided a rather sharp contrast to bank portfolio additions in earlier years of the current expansion. Over the five years ended in December 1966, commercial banks liquidated \$10.4 billion of United

States Government securities, whereas in 1967 they increased their holdings of these securities by over \$6 billion.

In addition to their acquisitions of Government securities, bank holdings of other securities rose by \$11.7 billion in 1967—by far the largest annual ad-

**Chart 6. BANK CREDIT AND LIQUID ASSETS: The rate of growth of bank credit advanced sharply in 1967. This increase was primarily the result of a large rise in investments, in marked contrast to the previous year when total investments declined. Liquid assets held by the nonbank public also rose considerably over the year, reflecting rapid gains in the money supply, commercial bank time deposits, and savings at thrift institutions.**



Data are seasonally adjusted monthly figures expressed in terms of an index, with the value for December of the preceding year set equal to 100.

vance on record. These securities acquisitions dominated the growth of total commercial bank credit in 1967. Although the rate of growth tapered off toward the year-end, the 11 per cent advance in bank credit over the year was almost double the growth in 1966 and exceeded the 8½ per cent average annual growth rate during the years 1961-65. However, the growth of total credit in the economy did not match the rise in bank credit, and the latter accounted for over half of the total credit extended in 1967 as compared with a 25 per cent share in 1966.

Bank loans increased less in 1967 than in 1966, when the advance in loans accounted fully for the year's bank credit growth. The growth of business loans in 1967—over 9 per cent—was the lowest since 1963 and was considerably below the 13½ per cent growth in 1966. Even though tax borrowing by businesses was relatively heavy in the first half of 1967, banks reacted to increased reserve availability and the decline in market rates of interest by reducing their prime rate to 5¾ per cent in January and to 5½ per cent in March (a few banks reduced their prime rate to 5½ per cent in January). In the second half, business borrowing from banks advanced less rapidly than in the first half, partly because tax liabilities were smaller and corporations held larger amounts of Government securities and certificates of deposit (C/D's) which matured near the tax dates.

The improvement of commercial bank liquidity in 1967 was evidenced in part by the dominance of Treasury securities acquisitions in the growth of bank earning assets. The ratio of loans to deposits, which is often used as a measure of bank liquidity, declined significantly during the year. Moreover, the growth in term loans moderated, and banks stepped up purchases of commercial paper and bankers' acceptances, further improving the liquidity of their earning assets.

The strong expansion of bank credit during 1967 was paralleled by a rapid increase in the money supply—private demand deposits and currency in circulation—and in commercial bank time deposits. The money supply plus time deposits increased by 11 per cent in 1967, more than double the advance in the previous year. This growth in part reflected the public's large demand for liquidity, which was severely squeezed in 1966. The money supply, for example, had actually declined slightly during the second half of 1966 and rose only about 2 per cent over the year as a whole. In 1967, the money supply increased by 6½ per cent, although its growth slowed toward the end of the year. Part of the rapid expansion of bank deposits resulted from the heavy volume of Treasury

flotations, concentrated in the second half of 1967, much of which was financed initially by commercial banks.

Time deposits at commercial banks increased by 16 per cent in 1967, almost double the rise in the preceding year. Commercial banks more than recouped their 1966 losses of large-denomination C/D's by February and, despite little C/D growth in the second quarter (maturing certificates were used for heavy accelerated tax payments), large-denomination C/D's outstanding at the end of 1967 were \$5 billion greater than at the end of the previous year. Consumer-type time deposits continued to climb throughout 1967, but not at the expense of passbook savings accounts which reversed their downward trend of the previous year. The high rate of personal saving and the desire of the public to rechannel its savings from open market instruments to more liquid bank deposits enhanced the growth of these funds.

The attractiveness of deposits at thrift institutions also revived considerably in 1967, as the public sought liquid assets and as market interest rates declined during the first part of the year from their 1966 highs. Consequently, inflows to mutual savings banks and savings and loan associations were much greater in 1967 than in 1966. Over the year, savings at the two types of institutions combined increased by 9 per cent, a much larger gain than in 1966. While the rate of increase of deposits diminished somewhat in the fourth quarter, when the yield differential became less advantageous, it was still well above the growth rate of the previous year. Mortgage credit extended by thrift institutions advanced more slowly than their deposits in 1967, reflecting the employment of inflows to replenish liquidity positions and to repay debt. However, extensions of mortgage credit by both mutual savings banks and savings and loan associations advanced considerably more than in 1966.

The rapid growth in the money supply, commercial bank time deposits, and deposits at thrift institutions contributed largely to the sharp advance in total liquid asset holdings of the nonbank public. These holdings rose by 8 per cent in 1967, compared with an increase of only 5 per cent in 1966. The advance in nonbank liquid assets was greater than the growth of overall economic activity in 1967, suggesting that the public was able to rebuild its liquidity over the year. After declining steadily since the end of 1964, the ratio of liquid assets to GNP rose moderately in 1967.

## **THE INTERNATIONAL ECONOMY**

The international monetary system was subject to unusually severe pressures during 1967, culminating in the devaluation of the pound sterling in November and subsequently in a brief but intense speculative attack on the United States dollar and other currencies. Early in the year, sterling had staged a dramatic recovery in the exchange markets, as the United Kingdom's balance of payments continued to respond to the corrective program introduced in the summer of 1966. Nevertheless, despite determined efforts on the part of the British government to restore balance-of-payments equilibrium, a number of forces—some of them unforeseen and beyond the control of the authorities—converged early in the summer to bring about renewed payments difficulties. After midyear, confidence in sterling weakened steadily, and on November 18 the government announced the devaluation of the pound sterling. In the immediate aftermath of the sterling devaluation, other currencies became suspect. With the United States balance of payments continuing in substantial deficit, the dollar was particularly vulnerable, and speculative pressures turned against it, mainly in the form of a huge rise in gold purchases in the London market. The potentially adverse effects of these pressures were moderated by prompt coordinated central bank action in both the gold and foreign exchange markets and, as the year came to a close, these markets were calm. However, the severity of the pressures on the dollar made it abundantly clear that the United States would have to undertake strong action to reduce its balance-of-payments deficit. A drastic program to achieve immediate results was announced on the first day of 1968.

### **The Sterling Devaluation**

Following the emergence of a major sterling crisis in the early summer of 1966, the British authorities responded in July of that year with a comprehensive set of stabilization measures designed to cut back the inflated level of domestic demand,

hold the line on wages and prices, and provide the basis for a lasting solution to the balance-of-payments problem. Superimposed on earlier policies of credit and fiscal restraint, the July program had a quick and pervasive effect on internal demands and prices, and by the closing months of 1966 it had begun to exert a remedial effect on the balance of payments. Largely as the result of a turnabout in the trade balance, the current account moved into surplus, and there was an underlying improvement in the long-term capital account as well.

Although the trade balance moved into slight deficit in the early months of 1967, the overall balance on current and long-term capital account remained in surplus. At the same time, there was a massive reflux of short-term funds to London. These inflows, combined with a seasonal improvement in the payments position of the overseas countries of the sterling area, enabled the Bank of England to increase its reserves by substantial amounts during the early months of the year, even after repaying all its earlier drawings under the Federal Reserve swap facility, the special credits extended by the United States Treasury, and all the short-term credits provided by other central banks in the summer of 1966. The total repayments, together with the improvement in Britain's own reserve position, came to more than \$1.3 billion in the first quarter of 1967 alone.

This pattern of significant improvement was interrupted in the early spring, when the recession on the Continent was reflected in a further decline in British exports and there was a renewed surge of imports. The announcement of the April trade returns on May 11 came as a distinct disappointment, and was followed a few days later by President de Gaulle's negative remarks on Britain's application to join the Common Market. However, the resulting setbacks were absorbed without undue strain on Britain's reserves. On May 25, the United Kingdom repaid, six months ahead of schedule, \$405 million under a 1964 drawing from the International Monetary Fund (IMF) together with the whole amount (\$80 million) borrowed the same year from Switzerland.

Sterling was subject to major pressures early in June, with the sudden eruption of the Middle East crisis. At the same time, there was a brief surge in demand for gold in the London market. The uncertainties generated by the outbreak of hostilities weakened sterling, not only directly, but also indirectly through the Euro-dollar market where a sharp increase in rates added a further element of pressure. These dual pressures were met by a coordinated central bank response in both the exchange and Euro-currency markets and, with the cessation of hostilities on June 7, sterling staged a strong recovery. Although the immediate disturbances were quickly dealt with, the current-account deficit

widened still further during the summer months in the aftermath of the war in the Middle East. The shutdown of the Suez Canal and the resultant jump in sea freight rates added substantially to Britain's transportation payments abroad. In addition, the embargo by Arab countries on oil shipments to the United Kingdom necessitated increased petroleum purchases from relatively high-cost sources of supply, while the flow of British exports to the Far East was impeded by the closing of the Suez Canal. Quite apart from the direct effects of the Middle East disturbances on the current-account balance, the very threat of large withdrawals of sterling balances by Arab countries intensified market fears. With the growing realization of the extent to which the United Kingdom's balance of payments was vulnerable to the aftereffects of the Middle East crisis, confidence in sterling—already shaken by a succession of poor trade returns—was all the more difficult to sustain. To make matters worse, these difficulties came almost simultaneously with the beginning of an adverse seasonal swing in the payments position of the overseas sterling area. In order to cushion the reserve impact of these developments, the Bank of England began to draw on its swap line with the Federal Reserve in June and in subsequent months also made extensive use of its credit facilities with other central banks as confidence in the pound weakened.

As market pessimism increased, a large part of the funds that had moved into Britain during the early months of the year flowed back into the Euro-dollar market or were switched into other foreign currencies. These withdrawals contributed heavily to the availability of funds in the Euro-dollar market, where they were absorbed by United States banks and to a smaller extent by Japanese borrowers. With confidence in sterling at a low ebb, the discount on forward sterling widened considerably after midyear, and interest rates in Britain remained unattractive on a covered basis. While the adverse interest differential undoubtedly encouraged some outflows from Britain, the withdrawal of funds was clearly dominated by the loss of confidence that developed following the Middle East crisis.

Against this background, the outbreak of dock strikes in London and Liverpool in September came as another damaging blow. As the strikes dragged on into November, sterling was heavily sold in both the spot and forward markets. In addition, the market increasingly questioned whether sterling's financial defenses would not simply collapse for lack of outside assistance. Although, in fact, additional assistance was available in substantial amounts even in the final hours of the crisis, there was no immediate prospect of a quick improvement in Britain's

balance of payments. Economic activity was still sluggish in a number of Britain's principal export markets on the Continent, and five months after the Middle East hostilities had broken out there were still no signs that the Suez Canal would be reopened. Above all, domestic considerations made it increasingly difficult for the government to take, at the existing parity, the measures required to restore equilibrium.

The government of the United Kingdom decided to terminate the struggle to maintain the parity of the pound at \$2.80 and on November 18 announced a devaluation of 14.3 per cent to \$2.40. In order to take full advantage of the competitive gain achieved through the devaluation—made all the greater by the fact that no other major industrial country devalued its currency—the United Kingdom reinforced its earlier policies of monetary and fiscal restraint to stimulate a shift of real resources into exports or import-competing industries. Simultaneously with the devaluation, the bank rate was raised from 6½ per cent to 8 per cent (the highest level since 1914), and the existing severe restrictions on bank and nonbank lending were further tightened. In order to bolster confidence in the new sterling parity, the IMF gave swift approval to the United Kingdom's November request for a \$1.4 billion standby credit and more than \$1.5 billion of credit facilities was made available by foreign central banks. To help the IMF finance United Kingdom drawings under the standby, should they prove necessary, the creditor countries in the Group of Ten—the ten leading industrial members of the Fund—agreed to lend the equivalent of \$525 million in their own currencies to the IMF under the General Arrangements to Borrow.

## **International Monetary System: Cooperation and Reform**

The devaluation of the pound was accomplished with a minimum disruption of the pattern of exchange rates. Within twenty-four hours after the devaluation, all the major industrial countries announced that they would maintain their currencies at existing parities, and currency readjustments were confined to a limited number of smaller countries. Nevertheless, fears that the devaluation of the pound might touch off a wider round of currency readjustments, as it did

in 1949, swept through the gold and foreign exchange markets. The nervousness in these markets clearly called for cooperative measures to minimize the spread of pressure to the dollar and to other currencies.

In the week after the devaluation, there was an enormous surge in private demand for gold in the London market, which reached new heights each day through Friday, November 24. In addition to doubts about the strength of the dollar, the demand was swollen by reports, subsequently confirmed, that earlier in the year France had withdrawn from the Gold Pool, an arrangement among central banks designed to keep the price of gold in the London market at a level close to the monetary price of gold. The speculative atmosphere faded in the following week after the governors of the central banks participating in the Gold Pool had reaffirmed their support for the present pattern of exchange rates based on the fixed price of \$35 per ounce of gold. At about the same time, the large Swiss commercial banks, acting at the request of the Swiss National Bank, announced that they would not accept orders to buy gold for foreign banks and also took steps to curtail credit for gold purchases by other parties. Similar measures were undertaken shortly thereafter by commercial banks in several other countries at the request of their respective central banks.

The rush into gold in November was accompanied by heavy flows of funds out of the Euro-dollar market into Continental currencies, particularly German marks. These movements contributed to an abrupt increase in Euro-dollar rates, and carried the mark and other currencies to substantial premiums in the forward market. In order to calm market fears and at the same time to ease the strains on the Euro-dollar market, a number of Continental central banks were prepared to provide forward cover for dollar investments. The German Federal Bank, for example, announced its willingness to buy dollars for future delivery in swap operations with commercial banks at rates designed to provide the banks with an incentive to move funds into the Euro-dollar market. In response to this incentive, the German commercial banks increased their dollar investments substantially. Acting on behalf of the United States authorities, the National Bank of Belgium, the Netherlands Bank, and the Swiss National Bank also undertook forward operations to reduce the strains in the exchange and Euro-dollar markets. In a related move, designed to give further assurance to the market of the determination of the monetary authorities to contain disruptive forces in the exchange markets, the Federal Reserve's swap lines with eight central banks and the Bank for International Settlements (BIS) were increased by a total of \$1.75 billion at the end of November.

Around mid-December there was a renewed increase in the speculative demand for gold, caused by fears that access to the London gold market would be restricted. The dollar again weakened very briefly against most major European currencies. However, the demand for gold returned to more normal levels after the United States authorities stated that the operation of the London gold market would remain unchanged and reiterated their determination to maintain the present price of gold. This statement also confirmed the fact that the central banks of the Gold Pool countries would continue to cooperate with the United States in the interest of maintaining the stability of the international monetary system. The expectation that the United States authorities would soon back up this statement with a strong program to reduce the payments deficit also had a calming effect on the markets.

Both before and after the devaluation of the pound sterling, the Federal Reserve System's network of reciprocal currency arrangements was extended and strengthened. In May, new swap facilities were negotiated with the central banks of Denmark and Norway in the amount of \$100 million each and with the Bank of Mexico for \$130 million. Then in July, against the background of the Middle East crisis, the Federal Reserve concluded increases of \$50 million each in its existing Swiss franc swap lines with the Swiss National Bank and with the BIS. At the same time, the System's swap facility with the BIS in other European currencies was increased by \$100 million to \$300 million. As already noted, swap lines were substantially enlarged at the end of November, raising the total of all arrangements to \$6,780 million, and in mid-December the Federal Reserve's Swiss franc swap lines with the Swiss National Bank and the BIS were each increased by \$150 million. At the year-end, the swap network of the Federal Reserve System with the central banks of fourteen countries and the BIS provided \$7,080 million in readily available resources to deal with short-term pressures in the exchange markets—as against \$4,500 million a year earlier.

In addition to the expansion of bilateral central bank credit facilities, international financial cooperation was evident in a number of other developments during 1967. Thus, in order to help neutralize the immediate balance-of-payments effects of United States military expenditures in Germany, the German Federal Bank agreed to invest \$500 million (in four equal quarterly instalments) in medium-term, mark-denominated securities issued by the United States Treasury. The first \$125 million security was issued in July and another in October. The German Federal Bank also stated that it would continue to refrain from converting dollars into gold at the United States Treasury. In another ex-

pression of international monetary cooperation, the Canadian authorities sold a total of \$150 million in gold to the United States during 1967, even though the Canadian balance of payments moved into surplus in the course of the year, and also purchased a \$200 million medium-term nonmarketable bond from the United States Treasury. Purchases of special Treasury securities were made by the central bank of Belgium and by the BIS.

A major benchmark in the evolution of the international monetary system was reached in September, when the board of governors of the IMF unanimously agreed on a plan for establishing special drawing rights (SDR's) in the IMF, and when needed, to supplement existing reserve assets—gold, foreign exchange, and reserve claims on the Fund. In working out the proposal, it was agreed that the new SDR's would be created by a decision taken by a substantial majority of the participants, for the purpose of meeting the reserve needs of the world as a whole and should not be geared to, or directed to, the financing of balance-of-payments deficits of individual countries. It was also agreed that the plan would be established as a new and segregated special account in the IMF and that the additional reserve assets should be distributed to all members on the basis of IMF quotas. The plan for the creation of SDR's is to be incorporated in proposals for amendments to the Fund's Articles of Agreement not later than March 1968. The amendments will then be submitted to all the members of the IMF for ratification—a process that could be completed in 1968 or early in 1969. The process of embodying the plan in the necessary legal form of amendments is going forward in the Executive Board of the Fund.

## **The United States Balance of Payments: A Serious Setback**

The continuing efforts to reduce the United States balance-of-payments deficit suffered a setback in 1967. To be sure, the erosion of the trade surplus that had occurred in the two preceding years was arrested in the first half of 1967, as domestic demand pressures subsided. But for the year as a whole the trade balance failed to improve. As a result of this, plus the effects of the increasing scale of the United States commitment in Vietnam and unusually large out-

flows on a number of other accounts, the balance-of-payments deficit on the liquidity basis<sup>1</sup> increased to \$3.6 billion in 1967, after having been reduced to an annual average of less than \$1½ billion in 1965-66, and the balance on the official reserve transactions basis shifted into substantial deficit (see Chart 7). The liquidity deficit increased over the course of the year and was particularly large in the fourth quarter. United States gold losses were very substantial in the aftermath of the sterling devaluation. Although pressures in the gold market subsided as the year came to a close, the further deterioration in the United States reserve position dramatized the need to take strong action to reduce the United States payments deficit, and a comprehensive corrective program was set in motion at the start of 1968.

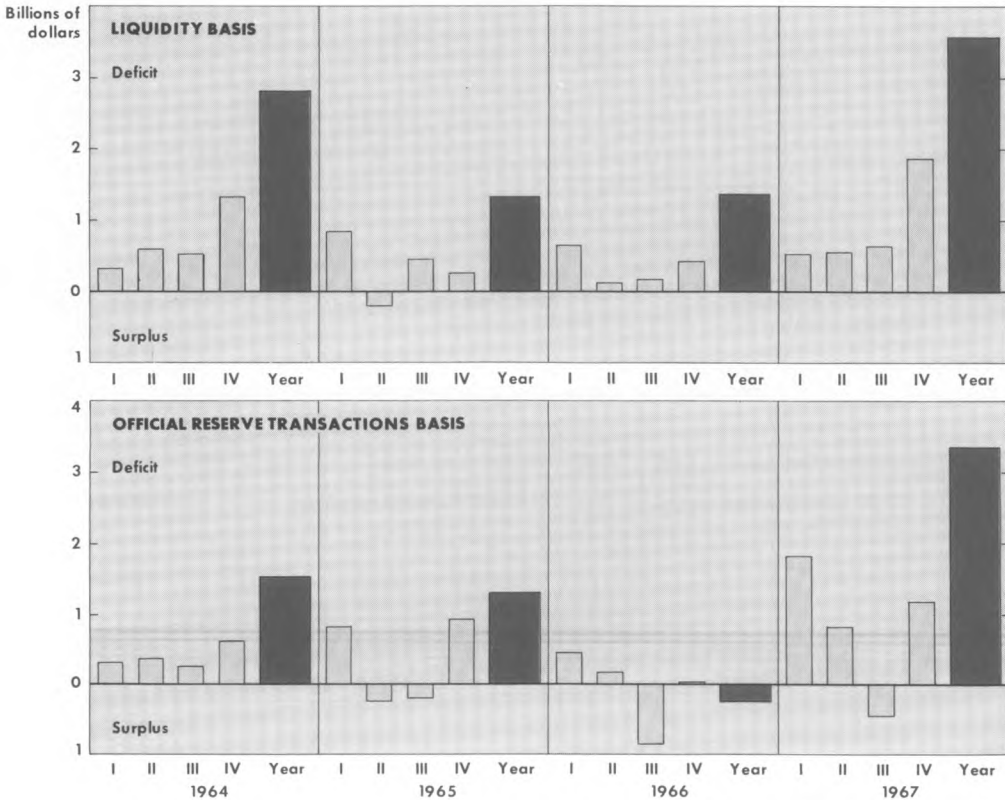
**SURPLUS ON GOODS AND SERVICES NARROWS.** With a slight reduction in the trade surplus accompanied by a further increase in military spending and other service payments abroad, the overall surplus on goods and services continued to shrink in 1967. Largely as a consequence of the more moderate pace of domestic business activity, the expansion of imports was interrupted during the first half of the year. The inventory adjustment then under way was accompanied by widespread reductions in imports of industrial raw materials and supplies. Similarly, purchases of imported machinery leveled off, as the pace of domestic capital investment slowed and domestic shortages eased somewhat. Once inventory investment began to accelerate, however, imports of raw materials began to increase, and in the latter half of the year there was a renewed advance in imports of capital goods as well. For 1967 as a whole, imports increased by about 5 per cent, after having increased by 19 per cent the year before when the pressure of excess demand was very strong.

The rate of increase in exports also slowed down considerably, compared with

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<sup>1</sup> The "balance on liquidity basis", published quarterly by the United States Department of Commerce in its Survey of Current Business, is the net sum of transactions in merchandise trade, services and transfers, United States private capital, United States Government grants and capital, foreign nonliquid capital, and unidentified transactions. When summed, these transactions equal the change, if any, in the United States international liquidity position, i.e., in United States monetary reserves and liquid liabilities to all foreigners. Another definition of the payments position published in the Survey is called the "balance on official reserve transactions basis". This definition differs from the "liquidity" balance in that changes in liquid liabilities to private foreigners and nonmonetary international organizations are put "above the line", and certain nonliquid liabilities to official foreigners are put "below the line". Hence, this balance is measured by changes in United States monetary reserves and changes in liquid and certain nonliquid liabilities to official foreigners.

**Chart 7. UNITED STATES BALANCE-OF-PAYMENTS DEFICIT: The payments deficit, on the liquidity basis, increased to \$3.6 billion in 1967, with a marked deterioration in the fourth quarter of the year. On the official reserve transactions basis, the balance shifted from a slight surplus in 1966 into a massive deficit in 1967, reflected in a sharp decline in United States gold stock toward the end of the year and in a large rise in United States liquid dollar liabilities to foreign official institutions.**



Quarterly data are seasonally adjusted.

the advance of 10 per cent in 1966. To some extent, this development reflected a reduction in aid-financed and other shipments of agricultural products. But more fundamentally the slower rise in exports was a natural concomitant of a widespread pause in the expansion of economic activity in a number of industrial

countries abroad. Indeed, virtually all the year-to-year gain in exports was concentrated in the first quarter, when the reduced pressure of domestic demand facilitated a rise in some nonagricultural exports, and there was a resurgence of shipments to the United Kingdom. Over the rest of the year, exports remained even with or below the first-quarter level. Although exports to Canada picked up as the year progressed and sales to Japan increased considerably, shipments to Western European countries, after having fallen sharply in 1966, remained substantially below their earlier peaks.

In addition to the disappointing results on trade account, there was a further substantial increase in military spending abroad associated with the enlarged conflict in Vietnam. On a global basis, expenditures overseas for military purposes rose to more than \$4 billion during 1967, with expenditures related to southeast Asia alone rising to a level about \$1.5 billion more than in 1964, the last full year before the military buildup. During the first half of 1967, the effects of rising military spending abroad on the current-account balance were mitigated through offsetting purchases of military equipment by foreign governments, but these purchases began to fall off around midyear, and for the year as a whole net military spending abroad continued to rise.

At the same time, net receipts from services declined somewhat, after having leveled off in 1966. This change was related, at least in part, to a number of special or temporary factors which had an adverse effect on both receipts and payments. In particular, there was an unusually rapid and much more than seasonal increase in foreign travel expenditures from May through October, as the centennial exposition in Canada attracted large numbers of United States tourists. Private United States remittances abroad also rose significantly, largely as a result of increased transfers to Israel. On the receipts side, United States income from direct investment abroad rose only slightly in 1967, possibly reflecting the delayed effects of a squeeze on profit margins in a number of Western European countries.

**CAPITAL OUTFLOWS INCREASE.** The outflow of United States private capital increased considerably in 1967, thus adding further to the pressures on the overall balance. New foreign securities issued in the United States, mainly by Canadian provincial and municipal governments and businesses, increased much more rapidly than in 1966. In the earlier months of the year, as interest rates in the United States moved sharply lower, there was a bulge of new Ca-

nadian bond issues, some of which had been postponed from 1966 when capital markets were tight. Canadian borrowings in the New York market tapered off in the summer only to increase once again in the fall, when conditions in the Canadian capital markets became congested. For the year as a whole, net United States purchases of new and outstanding long-term foreign securities increased to about \$1.1 billion, compared with only \$0.5 billion in 1966. Moreover, short-term bank-reported credits to foreigners increased by almost \$800 million, as Japanese importers and other foreign borrowers again turned to the United States money market to meet part of their financing requirements. By contrast, in 1966, when interest rates were somewhat lower in Japan and considerably higher in the United States, Japanese borrowers had made net repayments of outstanding loans and credits. Foreign affiliates of United States corporations continued to increase their spending for plant and equipment in 1967, though not so rapidly as in earlier years. In response to the Commerce Department's program to limit direct investment outflows, United States corporations borrowed about \$450 million abroad through new securities issues, mostly in Europe, and total direct investment outflows, net of the use of proceeds of such borrowings, were below the \$3.1 billion 1966 outflow.

**FINANCING THE DEFICIT.** The payments deficit was almost fully reflected in a massive buildup of the United States liquid liabilities to foreigners, which rose by about \$3.5 billion. United States reserve assets dropped by less than \$100 million for the year as a whole. A decline in the gold stock was more than fully offset by a substantial increase in holdings of convertible currencies and by a small improvement in the United States position in the IMF.

However, the composition of the settlement items shifted substantially within the year, largely along with the change in the position of sterling. Thus, during the first half of 1967, United States official holdings of sterling were sharply reduced, as the Bank of England used some of its dollar accumulations to repay short-term assistance received earlier from the Federal Reserve and the United States Treasury. After the eruption of the Middle East disturbances, there was a substantial rise in United States holdings of convertible currencies, consisting largely of sterling acquired as the counterpart of the United Kingdom's drawings of dollars under its swap facility with the Federal Reserve. During the third quarter, the balance on official transactions (seasonally adjusted) moved into surplus, even though the deficit on the liquidity basis continued to rise. However,

in the fourth quarter, when the dollar was at times under severe pressure in the gold and foreign exchange markets, the balance on official settlements was in deficit by about \$1.2 billion.

Although United States gold holdings dropped by \$1,170 million for the year as a whole, almost all this decline occurred in December and largely reflected sales of gold through the Gold Pool, rather than gold purchases by foreign official institutions from the Treasury. Indeed, the amount of gold held by monetary authorities outside the Communist area declined further in 1967, as private absorption of gold remained substantially in excess of available supplies.

**THE 1968 BALANCE-OF-PAYMENTS PROGRAM.** The need for decisive action to reduce the payments deficit became increasingly urgent as the year drew to a close, and on January 1, 1968 President Johnson announced a series of drastic corrective measures including the introduction of mandatory restrictions on direct investment abroad. While these and other restraints are designed to reduce capital outflows to all areas, they apply with special severity to the developed countries of continental Europe—typically surplus countries in recent years.

The Federal Reserve guidelines for restraint of foreign credits by banks and other nonbank financial institutions, as announced on January 1, 1968, are much more restrictive than the guidelines issued in November 1967. For banks, the general ceiling on foreign credits was reduced to 103 per cent of their 1964 base, from the 109 per cent ceiling set in November. But, in addition, the banks were asked to reduce outstanding term loans to the developed countries of continental Western Europe and also to cut outstanding short-term credits to these countries by 40 per cent during the course of 1968, with each bank's general ceiling lowered by the amount of such reductions over the course of the year. Nonbank financial institutions were requested to reduce their holdings of certain foreign assets by 5 per cent during 1968 and also to repatriate all liquid assets not essential for the conduct of their foreign business. The new guidelines for bank and nonbank financial institutions are expected to achieve a net inflow of at least \$500 million during 1968, which would represent an improvement, by comparison with 1967 outflows covered by the program, of roughly \$900 million. However, the guidelines are so designed as to focus the effect of the reduction in loans on the developed countries of continental Western Europe and to minimize any adverse effects on export credits or on credits to developing

countries. Although the Federal Reserve program remained on a voluntary basis, the Board of Governors of the Federal Reserve System was given standby authority to invoke mandatory controls.

The Department of Commerce's guidelines for restraint of direct investment abroad were replaced by mandatory limitations on most direct investment outflows by American corporations. Net transfers of capital by United States investors for direct investment in all advanced continental European countries and South Africa are subject to a moratorium during 1968. For certain developed countries, such as Canada, Japan, the United Kingdom, and Australia, in which a high level of capital inflow is essential either for the maintenance of economic growth or for financial stability, the total of new capital transfers plus reinvested earnings may not exceed 65 per cent of the average of direct investment in these countries during 1965-66. The ceiling for the less developed countries as a group is, however, 110 per cent of the average in 1965-66. These regulations, together with an additional requirement that United States investors repatriate certain short-term financial assets held abroad, are expected to produce a \$1 billion improvement in the balance of payments during 1968.

In addition to the measures directed toward private capital outflows, the President requested a series of other programs to improve the surplus on current account. In particular, the President appealed to Americans to defer non-essential travel outside the Western Hemisphere and indicated that legislation would be introduced to help cut the travel deficit. Moreover, the President requested the Congress to earmark \$500 million of Export-Import Bank funds to provide improved export insurance, and generally broaden the scope of Government financing of United States exports, as part of a more comprehensive export-promotion program. Moreover, an intensive effort will be made to secure the removal by foreign surplus countries of certain nontariff barriers to trade, and thereby further the progress toward trade liberalization achieved under the Kennedy Round of tariff negotiations. At the same time, it was announced that negotiations would be initiated with NATO allies to offset the foreign exchange costs of United States military spending in Europe—a goal that could be achieved either by increasing their defense purchases in the United States or through investments in United States Treasury securities.

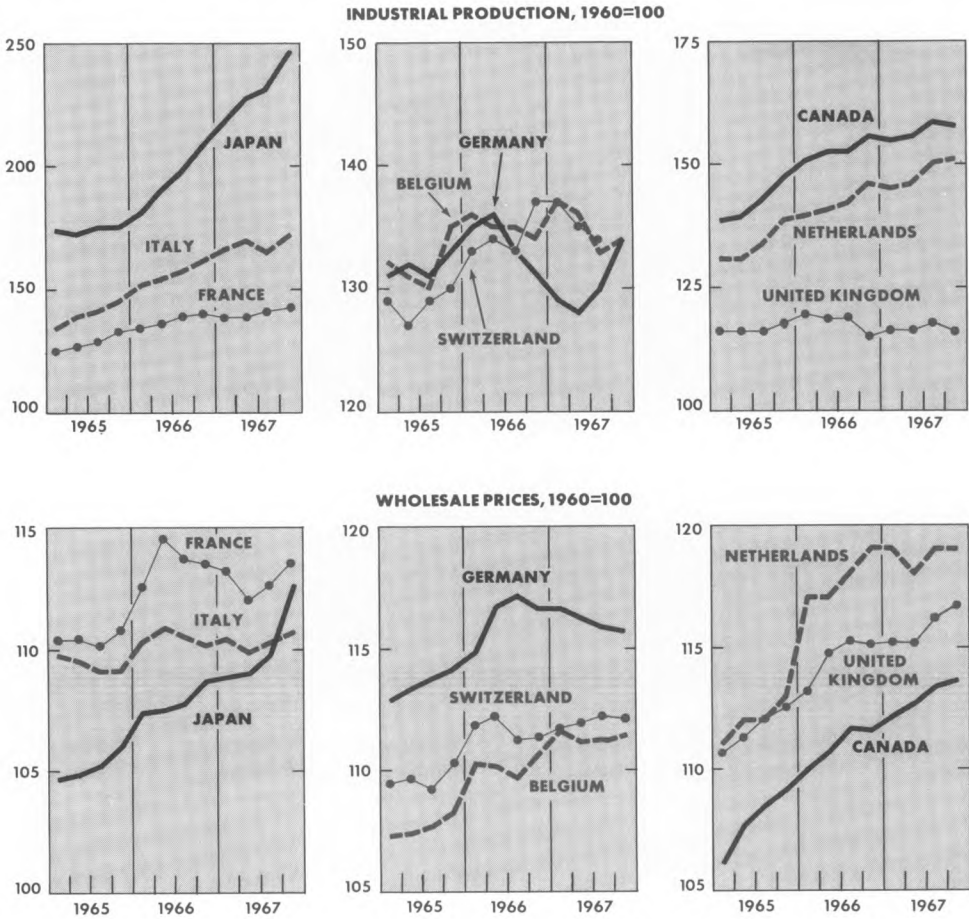
## **The Economic Slowdown in Industrial Countries Abroad**

As already noted, the relatively slow growth in United States exports in 1967 reflected a pronounced pause in the pace of economic activity in a number of industrial countries abroad (see Chart 8). The growth in real output, after having lost much of its upward momentum in 1966, came to a halt or slowed down considerably in the first half of 1967, as earlier policies of monetary restraint took full effect. The setback to expansion was most severe in Germany where the decline in business investment proceeded at an unexpectedly rapid rate in the latter half of 1966. In the United Kingdom, industrial production had dropped sharply after the July stabilization measures began to take hold. Because of Germany's importance as an export market, the decline in economic activity spread—with varying speed and intensity—to Belgium, Sweden, Austria, and several other European countries, while the slowdown in the United States around the end of 1966 was reflected in a concurrent pause in economic activity in Canada.

During the early months of 1967 the tensions in the money markets that had developed in 1966 were eased considerably, as a result of concerted action by monetary authorities in several countries designed to avoid a cumulative decline in output. In Germany, conditions in the financial markets had already been allowed to ease slightly in the latter half of 1966, when an increasing balance-of-payments surplus resulted in a large inflow of liquid funds. Shortly after the turn of the year, the German monetary authorities moved progressively toward a more active policy of monetary ease through successive reductions in the discount rate and minimum reserve requirements. In several other countries, notably Canada and Belgium, there was a rapid reversal of earlier policies of monetary restraint—a reversal marked by repeated reductions in central bank discount rates (see Chart 9). Following the relaxation of monetary restraint abroad and against a background of considerable progress toward the restoration of external balance, the Bank of England lowered the bank rate, in several steps, from the crisis level of 7 per cent to 5½ per cent in May.

The shift toward monetary ease in Germany was supported by a more flexible use of fiscal policy. The main fiscal stimulus was provided by the introduction of a special “contingency” budget in February, which called for a substantial increase in public investment. At the same time, the authorities introduced liberalized depreciation allowances for expenditures on fixed assets contracted before the end of October 1967. Moreover, in order to alleviate any

**Chart 8. PRODUCTION AND WHOLESALE PRICES IN INDUSTRIAL COUNTRIES ABROAD:** The pace of economic activity slowed down considerably in most major industrial countries abroad, and price rises were arrested in some countries. By the end of 1967, there were indications that economic recovery was under way in several countries.



Data for the fourth quarter of 1967 are estimated.

strains in the financial markets resulting from the government's increased borrowing requirements, the German Federal Bank for the first time began to

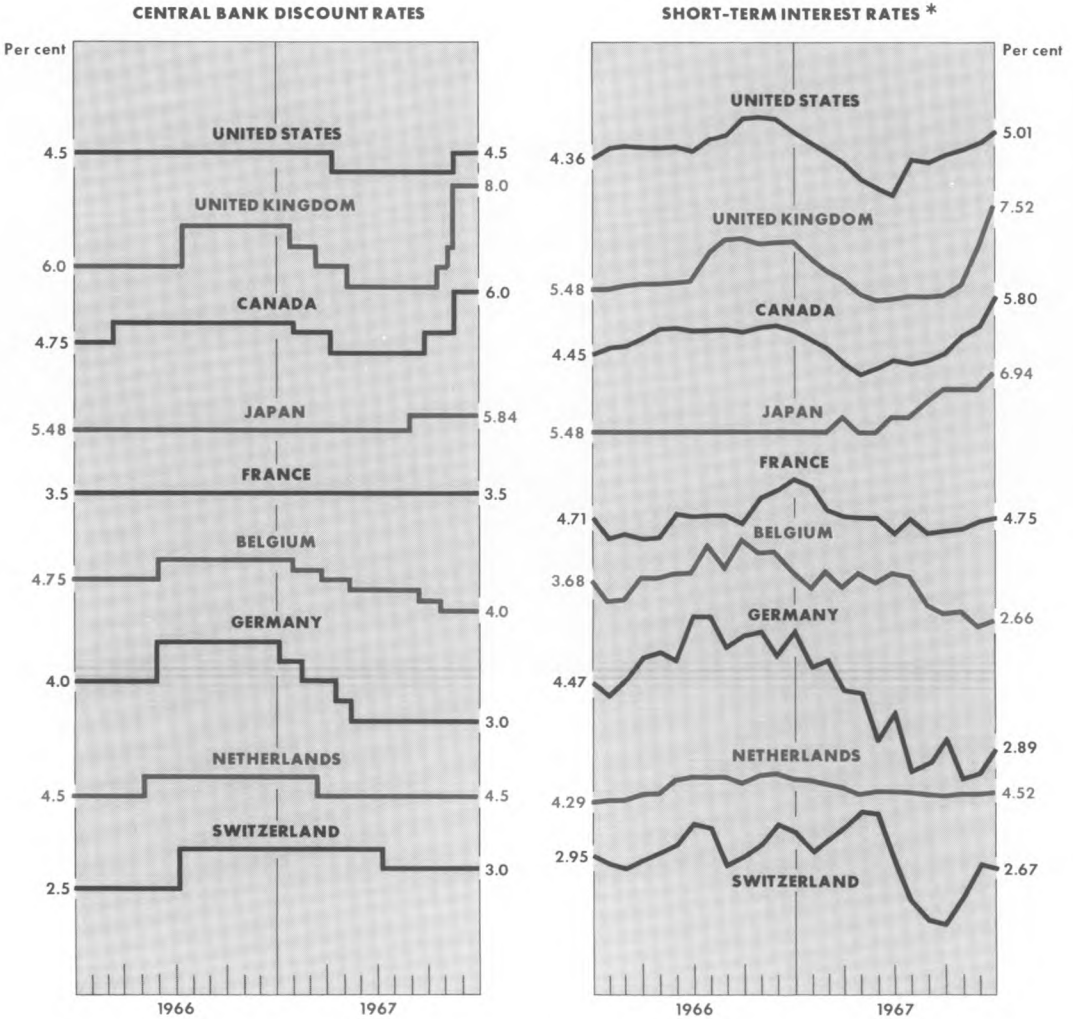
purchase long-term government securities. The recession bottomed out in the spring, and in the latter half of the year there was a strong recovery in industrial production.

Elsewhere in Western Europe, the shift toward monetary ease was generally more cautious and brought little response in the form of renewed economic growth. In France, the expansion in overall demand began to slow down considerably at the start of 1967, as private consumption leveled off. The government adopted some measures during the summer to speed up public investment outlays and to reduce certain tax revenues, but these steps were partially offset by increased social security charges. Despite the softness in the economy, both short- and long-term interest rates remained at relatively high levels. In several of the smaller European countries—notably Sweden, the Netherlands, and Belgium—the maintenance of strongly anti-inflationary monetary policies until late 1966 reinforced the effects of a reduction in foreign demand for exports. Although monetary restraint was relaxed in each of these countries early in 1967, the use of expansionary fiscal measures was restrained by concern over actual or anticipated increases in costs and prices. In the United Kingdom, only the most cautious policy stimulants were undertaken in view of the persisting balance-of-payments problem.

Among the major industrial countries, only Italy and Japan enjoyed a substantial upswing in activity throughout the year. In Italy, where cyclical developments have been out of phase with those in other Continental countries for the past three years, the trade deficit widened considerably and the overall payments surplus continued to decline. Similarly, in Japan the trade balance shifted into substantial deficit, as the upswing gathered momentum and inflationary pressures intensified. Despite a substantial increase in short-term borrowing in the form of acceptance credits from the United States, Japan's balance of payments moved into deficit.

The Canadian economic situation and the policies adopted to meet it altered in the course of 1967. Early in the year, as the pace of the business expansion slowed down, monetary policy shifted toward ease, and this shift was accompanied by the removal in April of earlier fiscal restraints on business investment. Despite the moderate growth in final demand, however, the average increase in wages continued to be far in excess of productivity gains and upward pressures on prices remained very strong. At the end of November, the Canadian government responded to these difficulties with restrictive fiscal measures, including a 5 per cent surcharge on personal income taxes and an acceleration of

**Chart 9. CENTRAL BANK DISCOUNT RATES AND SHORT-TERM INTEREST RATES:** The first half of 1967 saw widespread reductions of short-term interest rates from the record levels reached in 1966, but this decline proved short-lived in most countries as monetary policy was subsequently tightened.



\* Three-month Treasury bill rates for the United States, Canada, the United Kingdom, and the Netherlands, and call money rates for other countries.

tax payments on corporate profits.

The changing pattern of economic conditions in the major industrial countries abroad was accompanied by substantial shifts in the trade balances of a number of these countries. However, in most cases the combination of policies adopted in 1967 made only a limited contribution to the reduction of international payments disequilibrium, and almost all the continental European countries remained in substantial payments surplus. Although the United States and other deficit countries have a responsibility for the correction of their payments imbalances, that responsibility is shared by the surplus countries as well.

## **THIS BANK'S OPERATIONS**

### **Volume and Trend of the Bank's Operations**

The volume of operations in many departments of the Bank expanded moderately in 1967. This expansion essentially reflected the continued growth in the domestic economy and the concomitant increase in the Bank's activities connected with the transfer of funds for the public.

Both the number and the dollar amount of checks processed by this Bank again reached record levels in 1967. Although the dollar amount of United States Government checks handled increased by only 3.7 per cent, the number of such checks rose by 5.3 per cent to 67 million. Some 806 million other checks—checks drawn on commercial banks and on this Bank—were handled during the year, a growth of 4.7 per cent over 1966. However, the dollar volume of such checks processed during 1967 jumped 27.8 per cent to reach \$753 billion. In part, the faster growth of the dollar volume of checks processed, by comparison with the increase in the number of checks handled, reflected an increase in the number of checks handled in packaged form. Regardless of the dollar amount of checks contained in a package, each package is counted as only one item in determining the number of checks handled. In addition, the dollar amount of checks drawn on this Bank increased by 31.4 per cent after having declined by some 18 per cent in 1966.

During 1967, the check collection function of this Bank continued to reap the benefits of the significant advances made in high-speed processing over the last few years. In December, for instance, 93 per cent of all checks received were processed by this Bank on high-speed equipment, compared with 91 per cent in December 1966. Almost 100 per cent of the checks handled by this Bank were preprinted, or post-encoded, with the routing symbol transit numbers of the drawee banks in Magnetic Ink Character Recognition (MICR) symbols. Indeed, of the 3.1 million checks processed daily by this Bank, only an average of about 1,400 checks failed to meet this Bank's processing requirements with respect to the MICR enscribing of the routing symbol transit number.

The use of this Bank's wire transfer facilities grew further in 1967, in a continuation of the trend that has been evident in recent years and which is prob-

**SOME MEASURES OF THE VOLUME OF OPERATIONS OF  
THE FEDERAL RESERVE BANK OF NEW YORK** (Including Buffalo Branch)

<b>Number of pieces handled</b> (in thousands)*	<b>1967</b>	<b>1966</b>
Currency received .....	1,568,138	1,469,135
Coin received† .....	1,552,479	1,462,830
Gold bars and bags of gold handled .....	240	347
Checks handled:		
United States Government checks .....	67,299	63,933
All other .....	805,555	769,653
Postal money orders handled .....	27,939	29,792
Collection items handled:		
United States Government coupons paid .....	3,507	3,713
Credits for direct sendings of collection items .....	324	337
All other‡ .....	23,989	21,763§
Issues, redemptions, exchanges by fiscal agency departments:		
United States savings bonds and notes   .....	31,053	30,831
All other obligations of the United States .....	9,395	9,895
Obligations of Federal agencies .....	142	142
Obligations of international organizations .....	114	76
Safekeeping of securities:		
Pieces received and delivered .....	8,997	10,148§
Coupons detached .....	8,760	5,131
Wire transfers of funds   .....	1,219	1,123
<b>Amounts handled</b> (in millions of dollars)		
Discounts and advances& .....	12,331	31,148
Currency received .....	10,828	10,187
Coin received† .....	180	167
Gold bars and bags of gold coin handled .....	3,341	4,912
Checks handled:		
United States Government checks .....	30,586	29,482
All other .....	752,946	589,059
Postal money orders handled .....	595	604
Collection items handled:		
United States Government coupons paid .....	3,400	3,132
Credits for direct sendings of collection items .....	1,054	826
All other‡ .....	3,884	3,528§
Issues, redemptions, exchanges by fiscal agency departments:		
United States savings bonds and notes   .....	1,686	1,768
All other obligations of the United States .....	668,493	612,503
Obligations of Federal agencies .....	7,625	7,564
Obligations of international organizations .....	1,499	925
Safekeeping of securities:		
Par value pieces received and delivered .....	845,143	785,281
Wire transfers of funds   .....	2,395,915	2,127,906

\* Two or more checks, coupons, etc., handled as a single item are counted as one "piece".

† Excludes shipments of new coin from the Mint.

‡ These figures include food stamps redeemed.

§ Revised.

|| Savings notes were issued beginning May 1, 1967 but will not be eligible for redemption until May 1, 1968.

¶ Excludes Treasury transfers between Federal Reserve Districts.

& The number of discounts and advances handled in 1967 was 937, compared with 2,698 in 1966.

ably in good part related to the sustained broadening of the interbank Federal funds market. While the rate of growth in the number of items transferred slowed somewhat in 1967, it still remained substantial. The dollar volume of wire transfers (excluding Treasury transfers between Federal Reserve Districts) increased by 12.6 per cent to reach \$2,396 billion, while the number of transfers advanced by 8.6 per cent to 1.2 million.

Coin receipts (other than shipments of new coin from the Mint) increased once again in 1967. This Bank received 1,552 million pieces of coin during the year, an increase of 6.1 per cent over 1966, while the dollar volume reached \$180 million, 7.8 per cent greater than in 1966. Since mid-1967, at the request of the United States Treasury, this Bank has been paying out only clad coins. All denominations of coins, with the exception of half-dollars, are now readily available. Half-dollars, however, continue to be allocated to banks on the basis of total deposits.

The total number of items handled in conjunction with the Bank's fiscal agency operations declined slightly in 1967. The number of obligations handled for the United States Government (other than United States savings bonds and notes), Federal agencies, and international organizations decreased by 4.6 per cent, but the corresponding dollar volume increased 9 per cent to reach \$678 billion.

Aggregate Second District member bank borrowings from this Bank declined sharply from the postwar high of \$31.1 billion reached in 1966, reflecting the ready availability of bank reserves that prevailed throughout most of the year and a consequent reduction in the need for banks to turn to the discount window. Total member bank borrowings fell to \$12.3 billion in 1967, 60.4 per cent below their 1966 level. As a result, the number of discounts and advances declined 65 per cent, from 2,698 to 937, with only 40 per cent of member banks borrowing as compared with 52 per cent in 1966.

Total holdings of gold, dollar balances, and other assets for foreign and international accounts rose to a record \$30.6 billion by the end of the year, an increase of \$2.3 billion over 1966. Holdings for international organizations were slightly lower at \$9.4 billion, but holdings for foreign accounts—at \$21.2 billion—were higher by about \$2.4 billion, reflecting the very heavy inflows of dollars into foreign central banks in the latter part of 1967. The bulk of the increase was in the form of United States Government securities.

During 1967 there were some further small purchases of gold from the United States in connection with International Monetary Fund quota increases,

offset by IMF deposits of gold with the Federal Reserve Bank of New York. These "mitigated" gold transactions began in September 1965, and as of December 31, 1967 the Bank held for United States Treasury account \$233.1 million of gold so deposited by the Fund, a small increase over such deposits held at the end of 1966.

This Bank continued to be a popular source of information on economic affairs. During 1967, the staff delivered 240 speeches to various business and educational groups, over one million copies of a wide variety of bank publications were distributed, and 13,015 visitors were received for tours.

During the year, the Payments Mechanism and Communications Development function was created to handle the Bank's long-range planning efforts in the computer-communications field. Employment at this Bank increased slightly in 1967, following declines in the preceding three years. At the end of 1967, total employment, including the officers and staff at the Head Office and the Buffalo Branch, stood at 3,993.

# Financial Statements

## STATEMENT OF EARNINGS AND EXPENSES FOR THE CALENDAR YEARS 1967 AND 1966 (In thousands of dollars)

	<b>1967</b>	<b>1966</b>
Total current earnings.....	556,220	485,347
Net expenses .....	44,392	41,395
	<hr/>	<hr/>
Current net earnings	511,828	443,952
Additions to current net earnings:		
Profit on sales of United States Government securities (net) .....	190	0
All other .....	381	395
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Total additions	571	395
Deductions from current net earnings:		
Loss on sales of United States Government securities (net) .....	0	622
All other .....	3	7
	<hr/>	<hr/>
Total deductions	3	629
Net additions or deductions (—).....	568	— 234
	<hr/> <hr/>	<hr/> <hr/>
<b>Net earnings available for distribution</b>	<b>512,396</b>	<b>443,718</b>
Dividends paid .....	9,093	8,770
Payments to United States Treasury (interest on Federal Reserve notes) .....	497,337	431,063
Transferred to surplus .....	5,966	3,885
<b>SURPLUS ACCOUNT</b>		
Surplus — beginning of year.....	148,348	144,463
Transferred from net earnings for year.....	5,966	3,885
	<hr/> <hr/>	<hr/> <hr/>
<b>Surplus—end of year</b>	<b>154,314</b>	<b>148,348</b>

**STATEMENT OF CONDITION**

(In thousands of dollars)

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<b>Assets</b>	<b>DEC. 31, 1967</b>	<b>DEC. 31, 1966</b>
Gold certificate account.....	2,320,058	2,048,010
Redemption fund for Federal Reserve notes.....	471,599	443,812
Federal Reserve notes of other Banks.....	173,044	189,085
Other cash .....	43,380	31,317
<b>Total cash</b>	<b>3,008,081</b>	<b>2,712,224</b>
Discounts and advances.....	48,480	32,352
Acceptances .....	164,197	193,119
Federal agency obligations.....	37,800	33,800
United States Government securities.....	12,450,175	11,525,500
<b>Total loans and securities</b>	<b>12,700,652</b>	<b>11,784,771</b>
<b>Other assets:</b>		
Cash items in process of collection.....	2,083,443	1,993,690
Bank premises .....	9,681	9,358
All other★ .....	730,489	526,222
<b>Total other assets</b>	<b>2,823,613</b>	<b>2,529,270</b>
<b>Total Assets</b>	<b>18,532,346</b>	<b>17,026,265</b>

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★ Includes assets denominated in foreign currencies and IMF gold deposited.

**STATEMENT OF CONDITION**

(In thousands of dollars)

<b>Liabilities</b>	<b>DEC. 31, 1967</b>	<b>DEC. 31, 1966</b>
Federal Reserve notes.....	9,853,951	9,238,183
Deposits:		
Member bank reserve accounts.....	5,994,388	5,277,742
United States Treasurer— general account.....	233,050	271,154
Foreign★ .....	31,835	55,965
Other† .....	463,763	396,432
<b>Total deposits</b>	<b>6,723,036</b>	<b>6,001,293</b>
Other liabilities:		
Deferred availability cash items.....	1,569,631	1,417,581
All other .....	77,100	72,512
<b>Total other liabilities</b>	<b>1,646,731</b>	<b>1,490,093</b>
<b>Total Liabilities</b>	<b>18,223,718</b>	<b>16,729,569</b>
<b>Capital Accounts</b>		
Capital paid in.....	154,314	148,348
Surplus .....	154,314	148,348
<b>Total Capital Accounts</b>	<b>308,628</b>	<b>296,696</b>
<b>Total Liabilities and Capital Accounts</b>	<b>18,532,346</b>	<b>17,026,265</b>
Contingent liability on acceptances purchased for foreign correspondents‡ .....	40,064	49,005
Ratio of gold certificate reserves to Federal Reserve note liability.....	28.3%	27.0%
★ After deducting participations of other Federal Reserve Banks amounting to	103,600	118,080
† Includes IMF gold deposit.		
‡ After deducting participations of other Federal Reserve Banks amounting to	115,810	141,548

## Changes in Membership

During 1967, the total number of member banks of the Federal Reserve System in this District declined from 399 to 383. The decrease in the number of member banks was the net result of the mergers of nineteen member banks and the organization of three new national banks. The 383 banks constitute 81 per cent of all commercial banks and trust companies in this District and hold 96 per cent of the total assets of all such institutions in this District.

### NUMBER OF OPERATING MEMBER AND NONMEMBER BANKS IN SECOND FEDERAL RESERVE DISTRICT AT THE YEAR-END

(Exclusive of savings banks, private banks, and industrial banks)

Type of Bank	DECEMBER 31, 1967			DECEMBER 31, 1966		
	Members	Non-members	Per cent members	Members	Non-members	Per cent members
National banks★ . . . . .	273	0	100	281	0	100
State banks and trust companies . . . . .	110	87	56	118	82	59
<b>Total</b>	<b>383</b>	<b>87</b>	<b>81</b>	<b>399</b>	<b>82</b>	<b>83</b>

★ Includes one national bank located in the Virgin Islands.

### CHANGES IN FEDERAL RESERVE MEMBERSHIP IN SECOND DISTRICT DURING 1967

<b>Total membership at beginning of year . . . . .</b>	<b>399</b>
<b>Increases:</b>	
New national banks . . . . .	3
<b>Decreases:</b>	
Member banks merged with other members . . . . .	17
Member banks merged with nonmembers . . . . .	2
<b>Total membership at the year-end</b>	<b>383</b>

## Changes in Directors and Officers

**CHANGES IN DIRECTORS.** In December, member banks in Group 1 elected R. E. McNeill, Jr., a Class A director and reelected Arthur K. Watson a Class B director, each for a three-year term beginning on January 1, 1968. Mr. McNeill, Chairman of the Board of the Manufacturers Hanover Trust Company, New York, N. Y., succeeded George A. Murphy, Chairman of the Board of the Irving Trust Company, New York, N. Y., who served for the three-year term that ended on December 31, 1967. Mr. Watson, Chairman of the Board, IBM World Trade Corporation, New York, N. Y., and Vice Chairman of the Board, International Business Machines Corporation, Armonk, N. Y., has been a Class B director since January 1965.

Also in December, the Board of Governors of the Federal Reserve System redesignated Everett N. Case as *Chairman* of the Board of Directors and *Federal Reserve Agent* for the year 1968. Mr. Case, President of the Alfred P. Sloan Foundation, New York, N. Y., has been a Class C director since January 1961. He served as *Deputy Chairman* in 1965 and as *Chairman* and *Federal Reserve Agent* in 1966 and 1967.

At the same time, the Board of Governors reappointed Kenneth H. Hannan *Deputy Chairman* for the year 1968. Mr. Hannan, Executive Vice President of the Union Carbide Corporation, New York, N. Y., served as a Class B director from January 1960 through 1965. In 1966, he was appointed a Class C director for a three-year term and served as *Deputy Chairman* in 1966 and 1967.

In December, the Board of Governors also reappointed James M. Hester a Class C director for the three-year term beginning on January 1, 1968. Dr. Hester, President of New York University, New York, N. Y., has been a Class C director since January 1965.

At the Buffalo Branch, the Board of Governors in November reappointed Robert S. Bennett a director of the Branch for a three-year term beginning on January 1, 1968. In December, the Board of Directors of this Bank redesignated Mr. Bennett as *Chairman* of the Branch Board for the year 1968. Mr. Bennett, General Manager of the Lackawanna Plant of the Bethlehem Steel Corporation, Buffalo, N. Y., has been a director of the Branch since January 1965 and served as *Chairman* of the Branch Board for the year 1967. In November, the Board of Directors of this Bank appointed Wilmot R. Craig and Charles L. Hughes as directors of the Buffalo Branch for three-year terms beginning on January 1, 1968. Mr. Craig, Chairman of the Board of the Lincoln

Rochester Trust Company, Rochester, N. Y., succeeded J. Wallace Ely, President of the Security Trust Company of Rochester, Rochester, N. Y. Mr. Hughes, President of The Silver Creek National Bank, Silver Creek, N. Y., succeeded John D. Hamilton, Chairman of the Board of the Marine Midland Chautauqua National Bank, Jamestown, N. Y. Messrs. Ely and Hamilton had served on the Branch Board since January 1965. In December, the Board of Governors appointed Norman F. Beach a director of the Buffalo Branch for the unexpired portion of a term ending on December 31, 1968. Mr. Beach, Vice President of the Eastman Kodak Company, Rochester, N. Y., succeeded Carl A. Day, Executive Vice President of Bausch & Lomb Inc., Rochester, N. Y., who had served on the Branch Board since January 1967 and who resigned, effective December 31, 1967, in anticipation of his retirement.

**CHANGES IN OFFICERS.** Since February 1967, one officer has retired and one officer has resigned:

Walter H. Rozell, Jr., Vice President in charge of Personnel and of Building Operating and Service, retired on special service retirement effective July 1, 1967. Mr. Rozell joined the Bank's staff in July 1932 and became an officer in January 1947. From November 1953 to February 1956, he was away from the Bank to serve as Governor of the State Bank of Ethiopia.

Frank W. Schiff, Assistant Vice President, resigned effective February 11, 1968 to accept appointment as Deputy Under Secretary of the Treasury for Monetary Affairs. Mr. Schiff joined the Bank's staff in July 1951 and became an officer in May 1958. From September 1964 until his resignation, he was on a leave of absence to serve as a senior staff member of the President's Council of Economic Advisers.

The following additional changes in the official staff, including the appointment of eight new officers and the reappointment of a former officer, have been made since February 1, 1967:

John J. Clarke, formerly Vice President and General Counsel, was appointed Vice President and Special Legal Adviser effective April 1, 1967. In this new position, Mr. Clarke is responsible for the Bank's long-range planning efforts in the computer-communications field, for coordinating such planning efforts with similar efforts within the Federal Reserve System and in the commercial banking system, and for the legal aspects of such long-range planning and of collection matters having System-wide importance.

Edward G. Guy, formerly Assistant General Counsel, was appointed Vice President and General Counsel effective April 1, 1967.

The appointment of Edward J. Geng as Assistant Secretary was terminated effective April 1, 1967, his appointment as Manager and assignment to the Securities Department continuing. Mr. Geng was appointed Assistant Vice President on January 4, 1968 and assigned to Open Market Operations and Treasury Issues.

James H. Oltman was appointed Assistant Secretary effective April 1, 1967, his appointment as Manager and assignment to the Bank Examinations Department continuing.

William H. Braun, Jr., Vice President in charge of Accounting and Planning, was also assigned responsibility for Building Operating and Service, effective May 5, 1967. Mr. Braun is now responsible for Administrative Services, comprising the Accounting, Building Operating, Computer Services, Management Information, and Planning Departments.

Thomas M. Timlen, Jr., Vice President in charge of Loans and Credits, was also assigned responsibility for Personnel, effective May 5, 1967. On January 4, 1968, the Service Department was transferred from the Administrative Services function to the Personnel function.

Richard G. Davis, formerly Manager, Domestic Research Department, was appointed Adviser effective July 1, 1967 and assigned to Research and Statistics. Mr. Davis had been on a leave of absence to serve as a Visiting Lecturer at Princeton University for the academic year 1966-67. He was appointed Assistant Vice President on January 4, 1968 and assigned to Research and Statistics.

Madeline H. McWhinney, formerly Manager, Statistics Department, was appointed Assistant Vice President effective July 1, 1967 and assigned to Research and Statistics, with responsibility for the Statistics Department.

Irving M. Auerbach, formerly Chief, Market Statistics Division, Statistics Department, was appointed an officer with the title of Manager effective July 1, 1967 and assigned to the Statistics Department.

Joseph R. Coyle, formerly Special Assistant, Securities Department, was appointed an officer with the title of Securities Trading Officer effective July 1, 1967 and assigned to the Securities Department.

Edna E. Ehrlich, formerly Chief, Balance of Payments Division, International Research Department, was appointed an officer with the title of Senior Economist effective July 1, 1967.

Peter D. Sternlight returned to the Bank on November 12, 1967, and was

reappointed an officer with the title of Assistant Vice President and assigned to Open Market Operations and Treasury Issues. Mr. Sternlight had resigned as an officer of the Bank in November 1965 to accept appointment as Deputy Under Secretary of the Treasury for Monetary Affairs, a position he held until November 11, 1967. Mr. Sternlight was appointed Vice President on January 4, 1968 and assigned to Open Market Operations and Treasury Issues, where he has supervisory responsibility for the operations of the function under Alan R. Holmes, Vice President.

Peter Fousek, formerly Assistant Vice President, was appointed Vice President on January 4, 1968 and assigned to Personnel, where he has supervisory responsibility for the operations of the function under Thomas M. Timlen, Jr., Vice President.

Bruce K. MacLaury, formerly Assistant Vice President, was appointed Vice President on January 4, 1968 and assigned to Foreign, where he has supervisory responsibility for the operations of the function under Charles A. Coombs, Vice President.

Spencer S. Marsh, Jr., formerly Assistant Vice President, was appointed Market Adviser on January 4, 1968 and assigned to Open Market Operations and Treasury Issues. In this new position, which is equivalent in rank to that of Vice President, Mr. Marsh is responsible for advice and special studies with respect to open market operations and policies.

David E. Bodner, formerly Manager, Foreign Department, was appointed Assistant Vice President on January 4, 1968 and assigned to Foreign.

A. Thomas Combader, formerly Manager, Building Operating Department, was appointed Assistant Vice President on January 4, 1968 and assigned to Administrative Services, with responsibility for the Building Operating Department.

Robert J. Crowley, formerly Manager, Foreign Department, was appointed Assistant Vice President on January 4, 1968 and assigned to Foreign.

John T. Arnold, formerly Special Assistant, Foreign Department, was appointed an officer with the title of Manager on January 4, 1968 and assigned to the Foreign Department.

Matthew C. Drexler, formerly Building Superintendent, Building Operating Department, was appointed an officer with the title of Manager on January 4, 1968 and assigned to the Building Operating Department.

Frederick L. Frey, formerly Supervising Examiner, Examining Division, Bank Examinations Department, was appointed an officer with the title of Chief

Examiner on January 4, 1968.

Benjamin Stackhouse, formerly Chief, Banking Facilities Division, Bank Examinations Department, was appointed an officer with the title of Manager on January 4, 1968 and assigned to the Bank Examinations Department.

Philip Van Orman, formerly Attorney, Legal Department, was appointed an officer with the title of Assistant Counsel on January 4, 1968.

Everett B. Post, Assistant Vice President assigned to Administrative Services, with responsibility for the Accounting and Planning Departments, was also assigned responsibility for the newly established Management Information Department, effective January 5, 1968.

Frederick L. Smedley, Assistant Vice President, formerly assigned to Personnel, and to Administrative Services with responsibility for the Building Operating and Service Departments, was assigned to Government Bond and Safekeeping of Securities effective January 5, 1968.

Gerald E. Beach, Manager, formerly assigned to the Government Bond and Safekeeping Department, was assigned to the Accounting Department and the Management Information Department effective January 5, 1968.

Robert L. Cooper, Manager, Acceptance Department, was also assigned to the Securities Department, effective January 5, 1968.

Martin French, Manager, formerly assigned to the Security Custody Department, was assigned to the Government Bond and Safekeeping Department effective January 5, 1968.

Aloysius J. Stanton, Manager, formerly assigned to the Accounting Department, was assigned to the Security Custody Department effective January 5, 1968.

**MEMBER OF FEDERAL ADVISORY COUNCIL—1968.** The Board of Directors of this Bank selected George S. Moore to serve during 1968 as the member of the Federal Advisory Council representing the Second Federal Reserve District. Mr. Moore is Chairman of the Board of the First National City Bank, New York, N. Y. He succeeded R. E. McNeill, Jr., Chairman of the Board of the Manufacturers Hanover Trust Company, New York, N. Y., who served as a member of the Council during 1967 and who has been a director of the Bank since January 1, 1968.

## Directors of the Federal Reserve Bank of New York

<b>DIRECTORS</b>	<i>Term expires Dec. 31</i>	<i>Class</i>	<i>Group</i>
R. E. MCNEILL, JR. .... Chairman of the Board, Manufacturers Hanover Trust Company, New York, N. Y.	1970	A	1
ROBERT G. COWAN .... Chairman of the Board, National Newark & Essex Bank, Newark, N. J.	1968	A	2
EUGENE H. MORRISON .... President, Orange County Trust Company, Middletown, N. Y.	1969	A	3
ARTHUR K. WATSON .... Chairman of the Board, IBM World Trade Corporation, New York, N. Y., and Vice Chairman of the Board, International Business Machines Corporation, Armonk, N. Y.	1970	B	1
MILTON C. MUMFORD .... Chairman of the Board, Lever Brothers Company, New York, N. Y.	1968	B	2
MAURICE R. FORMAN .... President, B. Forman Co., Inc., Rochester, N. Y.	1969	B	3
EVERETT N. CASE, <i>Chairman, and Federal Reserve Agent</i> .... President, Alfred P. Sloan Foundation, New York, N. Y.	1969	C	
KENNETH H. HANNAN, <i>Deputy Chairman</i> .... Executive Vice President, Union Carbide Corporation, New York, N. Y.	1968	C	
JAMES M. HESTER .... President, New York University, New York, N. Y.	1970	C	

### **DIRECTORS—BUFFALO BRANCH**

ROBERT S. BENNETT, <i>Chairman</i> .... General Manager, Lackawanna Plant, Bethlehem Steel Corporation, Buffalo, N. Y.	1970		
NORMAN F. BEACH .... Vice President, Eastman Kodak Company, Rochester, N. Y.	1968		
ARTHUR S. HAMLIN .... President, The Canandaigua National Bank and Trust Company, Canandaigua, N. Y.	1968		
GERALD F. BRITT .... President, L-Brooke Farms, Inc., Byron, N. Y.	1969		
E. PERRY SPINK .... Chairman of the Board, Liberty National Bank and Trust Company, Buffalo, N. Y.	1969		
WILMOT R. CRAIG .... Chairman of the Board, Lincoln Rochester Trust Company, Rochester, N. Y.	1970		
CHARLES L. HUGHES .... President, The Silver Creek National Bank, Silver Creek, N. Y.	1970		

### **MEMBER OF FEDERAL ADVISORY COUNCIL—1968**

GEORGE S. MOORE .... Chairman of the Board, First National City Bank, New York, N. Y.	1968		
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# Officers of the Federal Reserve Bank of New York

ALFRED HAYES, *President*  
WILLIAM F. TREIBER, *First Vice President*

HAROLD A. BILBY, *Vice President and Senior Adviser*  
WILLIAM H. BRAUN, JR., *Vice President*  
JOHN J. CLARKE, *Vice President and Special Legal Adviser*  
CHARLES A. COOMBS, *Vice President*  
FELIX T. DAVIS, *Vice President*  
PETER FOUSEK, *Vice President*  
GEORGE GARVY, *Economic Adviser*  
EDWARD G. GUY, *Vice President and General Counsel*  
MARCUS A. HARRIS, *Vice President*  
ALAN R. HOLMES, *Vice President*  
ROBERT G. LINK, *Vice President*  
BRUCE K. MACLAURY, *Vice President*  
SPENCER S. MARSH, JR., *Market Adviser*  
FRED W. PIDERIT, JR., *Vice President*  
PETER D. STERNLIGHT, *Vice President*  
THOMAS M. TIMLEN, JR., *Vice President*  
THOMAS O. WAAGE, *Vice President*

THOMAS C. SLOANE, *Assistant General Counsel*

DAVID E. BODNER, *Assistant Vice President*  
A. THOMAS COMBADER, *Assistant Vice President*  
ROBERT J. CROWLEY, *Assistant Vice President*  
RICHARD G. DAVIS, *Assistant Vice President*  
EDWARD J. GENG, *Assistant Vice President*  
PETER P. LANG, *Adviser*  
WILLIAM E. MARPLE, *Assistant Vice President*  
MADELINE H. McWHINNEY, *Assistant Vice President*  
PAUL MEEK, *Assistant Vice President*  
DONALD C. NILES, *Assistant Vice President*  
EVERETT B. POST, *Assistant Vice President*  
LAWRENCE E. QUACKENBUSH, *Assistant Vice President*  
KENNETH E. SMALL, *Assistant Vice President*  
FREDERICK L. SMEDLEY, *Assistant Vice President*  
GEORGE C. SMITH, *Assistant Vice President*  
ROBERT C. THOMAN, *Assistant Vice President*

JOHN T. ARNOLD,  
*Manager, Foreign Department*  
IRVING M. AUERBACH,  
*Manager, Statistics Department*  
GERALD E. BEACH,  
*Manager, Accounting Department, and  
Manager, Management Information Department*  
LEONARD I. BENNETTS,  
*Manager, Cash Custody Department, and  
Manager, Collection Department*  
LOUIS J. BRENDEL,  
*Manager, Planning Department*  
ROBERT L. COOPER,  
*Manager, Acceptance Department, and  
Manager, Securities Department*  
JOSEPH R. COYLE,  
*Securities Trading Officer*  
HOWARD F. CRUMB,  
*Manager, Computer Services Department*  
RICHARD A. DEBS,  
*Secretary, and Assistant Counsel*  
FREDERICK W. DEMING,  
*Manager, Securities Department*  
ADAM R. DICK,  
*Manager, Bank Relations Department*  
MATTHEW C. DREXLER,  
*Manager, Building Operating Department*  
KARL L. EGE,  
*Manager, Check Department*  
EDNA E. EHRLICH, *Senior Economist*  
MARTIN FRENCH,  
*Manager, Government Bond and  
Safekeeping Department*  
FREDERICK L. FREY, *Chief Examiner*  
RALPH H. GELDER,  
*Manager, Personnel Department*

RICHARD H. HOENIG,  
*Manager, Public Information Department*  
FRED H. KLOPSTOCK,  
*Manager, International Research Department*  
LEONARD LAPIDUS,  
*Manager, Bank Examinations Department*  
ROBERT MEYER, *Assistant Counsel*  
ARTHUR H. NOA,  
*Manager, Service Department*  
JAMES H. OLTMAN,  
*Manager, Bank Examinations Department, and  
Assistant Secretary*  
SCOTT E. PARDEE,  
*Manager, Foreign Department*  
EDWIN R. POWERS,  
*Manager, Foreign Department*  
CHARLES R. PRICHER,  
*Manager, Cash Department*  
A. MARSHALL PUCKETT, *Senior Economist*  
FRANCIS H. ROHRBACH,  
*Manager, Personnel Department*  
EDWIN S. ROTHMAN,  
*Manager, Foreign Department*  
HERBERT H. RUESS,  
*Manager, Credit and Discount Department*  
WALTER S. RUSHMORE,  
*Manager, Savings Bond Department*  
FREDERICK C. SCHADRACK, JR.,  
*Manager, Domestic Research Department*  
BETTY JEAN SHEA, *Assistant Counsel*  
BENJAMIN STACKHOUSE,  
*Manager, Bank Examinations Department*  
ALOYSIUS J. STANTON,  
*Manager, Security Custody Department*  
PHILIP VAN ORMAN, *Assistant Counsel*  
ROBERT YOUNG, JR., *Assistant Counsel*

JOHN P. JENSEN, *General Auditor*  
WILLIAM M. SCHULTZ, *Assistant General Auditor*

**OFFICERS — BUFFALO BRANCH**

ANGUS A. MACINNES, JR., *Vice President*  
JOHN T. KEANE, *Assistant Vice President and Cashier*

HARRY A. CURTH, JR., *Assistant Cashier*  
RONALD B. GRAY, *Assistant Cashier*

GERALD H. GREENE, *Assistant Cashier*  
ARTHUR A. RANDALL, *Assistant Cashier*

# THE SECOND FEDERAL RESERVE DISTRICT

