FORTY-EIGHTH

Annual Report

OF THE

BOARD OF GOVERNORS
of the Federal Reserve System

COVERING OPERATIONS FOR THE YEAR

1961

DIGEST OF PRINCIPAL FEDERAL RESERVE POLICY ACTIONS, 1961

Period	Action	Purpose of action
January	Limited net sales of U.S. Government securities from Federal Reserve portfolio to about $500 million. Member bank borrowing at Reserve Banks averaged only $50 million.	To encourage bank credit and monetary expansion by absorbing only part of seasonal inflow of reserve funds not otherwise offset by a large gold outflow.
February-August	Bought substantial amounts of U.S. Government securities with maturities over 1 year, following February 20 announcement that System open market operations would include securities outside the short-term area. These purchases were partly offset by net sales of short-term securities. Total System holdings of Governments increased about $700 million. Member bank borrowings averaged $75 million.	To encourage bank credit and monetary expansion while avoiding direct downward pressure on short-term interest rates, thereby moderating pressures on the U.S. balance of payments from outflow of short-term capital attracted by higher interest rates abroad.
September-December	Bought or sold at different times varying amounts of U.S. Government securities, including securities with longer maturities. Total System holdings of Government securities increased about $1.6 billion. Member bank borrowings at Reserve Banks remained generally low.	To continue to encourage bank credit and monetary expansion while allowing for changing reserve needs due to seasonal and other factors, including a large gold outflow, and while continuing to give consideration to the balance of payments problem.
December	Raised, effective Jan. 1, 1962, maximum interest rates payable by member banks on any savings deposit from 3 to 3½ per cent, and to 4 per cent on those left in the bank for 1 year or more; also raised maximum rates on time deposits with a maturity of 6 months to 1 year from 3 to 3½ per cent, and to 4 per cent on those deposits with a maturity of a year or longer.	To enable banks to compete more effectively for savings and other time deposits, including foreign time deposits, thus moderating pressures on the U.S. balance of payments, and, over the long run, to offer additional incentive for the accumulation of savings required for financing future economic growth.

Total bank credit expanded significantly in September and in the third quarter as a whole, the conventionally defined money supply showed in September the first substantial increase in several months, and time deposits at commercial banks continued their rapid growth. These developments were aided by substantial new cash offerings of Treasury securities, which had been acquired in large part by the banks. Treasury bills had been relatively firm, with 3-month bill rates moving generally within the 2.25 - 2.35 per cent range in which they had fluctuated since late August. Within about a week, the Treasury was expected to announce the terms of a large November refunding.

In the third quarter, transfers to foreigners of gold, convertible foreign currencies, and dollars were at a seasonally adjusted annual rate of more than $3 billion, as compared with an annual rate of less than $2 billion in the second quarter, after eliminating the influence of special debt repayments. Within the third quarter, moreover, September appeared to have been the weakest month, and such October figures as were available suggested little, if any, improvement. Whereas in the second quarter basic U. S. payments were approximately in balance, the third-quarter figures reflected a deficit. The main reasons for the deterioration were that imports had increased faster than expected and the net capital outflow had failed to diminish.

Consideration of these diverse factors resulted in a consensus that a continuation of the monetary policy the Committee had been following would be appropriate from the standpoint of domestic conditions, though with a tendency to resolve any doubts arising in the conduct of open market operations on the side of less ease. It was agreed that the System should meet seasonal needs for reserves and also that it should endeavor, in accordance with its practice of long standing, to maintain steady money market conditions in view of the Treasury's refinancing program. Because of international factors, however, the consensus favored giving more than usual attention to short-term rates.

Mr. Mills dissented from the implementation of policy in the

manner indicated by the consensus because, as he had indicated at the October 3 meeting, he felt that Federal Reserve policy aimed at encouraging the expansion of bank credit had resulted in an increase in banking, industrial, and commercial liquidity that was approaching an inflationary status and had already tended to damage the fabric of the money market. In the circumstances, including the ramifications of the international situation, he believed that a start should be made toward implementing a moderately restraining monetary and credit policy.

2. Authority to effect transactions in intermediate- and longer-term securities.

The Committee authorized the Federal Reserve Bank of New York, between this date and the next meeting of the Committee, within the terms and limitations of the directive issued at this meeting, to acquire intermediate- and/or longer-term Government securities of any maturity, or to change the holdings of such securities, in an amount not to exceed $500 million.

Votes for this action: Messrs. Hayes, Balderston, Irons, King, Mills, Mitchell, Shepardson, Swan, and Ellis. Votes against this action: Messrs. Allen and Robertson.

No changes were indicated in previously expressed positions of members of the Committee concerning the authorization and operations thereunder.

November 14, 1961

1. Authority to effect transactions in System Account.

The Committee renewed without change the directive to the Federal Reserve Bank of New York providing for open market operations with a view to encouraging credit expansion so as to promote fuller utilization of resources, while giving consideration to international factors.

Votes for this action: Messrs. Martin, Hayes, Allen, Irons, King, Mills, Mitchell, Robertson, Swan, and Wayne. Votes against this action: none.

On the basis of preliminary data, the Board's industrial production index appeared to have recovered in October the 1-point September decline, and possibly to have exceeded the August high. With the model changeover completed and the strike settled, automobile production had increased sharply in October, with a further substantial rise in November indicated by industry schedules. New orders for machinery were up in October, along with heavy engineering contracts, employment showed moderate improvement, and total retail sales had broken out of the narrow range within which they had fluctuated since midyear. The unemployment rate continued, however, at approximately the level that had persisted for almost a year. Some decline was noted in a few sensitive commodity prices, and third-quarter corporate profits were below earlier expectations. A recent private survey of business plans for spending on new plant and equipment in 1962 suggested only a modest rise above the level of expenditures for the current year. On the other hand, consumer spending showed signs of considerably improved strength in October.

Despite the October showing with regard to increased consumer spending, questions still remained concerning the underlying strength of consumer demand. For example, consumer savings and liquid asset holdings were still continuing at a high level, and consumers were not yet resorting actively to the use of their available borrowing power. The latest samplings of buying intentions for durable goods, moreover, afforded little evidence that consumer demand might become a strong independent factor in furthering economic expansion in the months immediately ahead.

In the financial area there had been a further sizable expansion in the money supply, accompanied by only a moderate increase in bank loans. The short-term Treasury bill rate had risen recently, following a downdrift in interest rates, particularly in the long-term sector. System open market operations during this period were large, but insufficient to meet the drain on reserves from market factors, and free reserves had declined somewhat, with modest tightening in the money market. While this

tightening had resulted from the play of market forces, circumstances such as the lower average free reserve figure for one of the statement weeks and the concurrent upward movement of Treasury bill rates had led to speculation regarding a shift in Federal Reserve policy.

Data on the U.S. balance of payments showed that for the third quarter of 1961 the deficit, on a seasonally adjusted basis, was at an annual rate somewhat above $3 billion, representing a substantial deterioration from the first half of the year. The largest single contributory factor to the increased deficit was a rise in imports. As to October, preliminary incomplete data afforded little basis for belief that the deficit had been reduced from the high September figure.

The consensus that evolved from the discussion at this meeting favored continuation for the period just ahead of a monetary policy calculated to produce approximately the same degree of ease that had prevailed for some time, except for the part of the preceding 3-week period in which a tendency toward a somewhat tighter money market had developed. It was the view of a majority of the Committee that, although economic developments should be watched closely in order to determine whether a shift in policy toward a less stimulative monetary posture would be appropriate, at this particular juncture various factors such as the persistence of a relatively high volume of unused resources, the absence of inflationary pressures, and the still unresolved question of the pace of consumer spending presented strong arguments against any significant lessening of monetary ease.

Two members of the Committee, Messrs. Hayes and Mills, dissented from the implementation of policy in the manner indicated by the consensus. Mr. Hayes felt that it would be desirable for the Treasury bill rate to move into a moderately higher range, as a contribution in a minor way toward recognition of the serious U. S. international payments problem, and he was prepared to accept a somewhat lower level of free reserves should that prove necessary to sustain the bill rate. However, he would not favor any noticeable shift in System policy at this time. Also, if the Treasury should decide to undertake an advance refunding in the near future, then he would feel that no change in existing monetary policy would be appropriate. Mr. Mills dissented because of his belief that implementation of policy according to the consensus would fail to take the initiative that the Federal Reserve System should properly take at this juncture. In his view the monetary and credit situation to which he had addressed himself at the two previous meetings of the Committee had since worsened. It continued to be imperative, in his opinion, to restrict the supply of reserves to such extent that the expansion of bank credit would be contained largely within the bounds of the resources already at the banks' disposal, at the same time that a firmer structure of interest rates would serve to discourage the transfer of gold and dollars abroad. In combination, the effect of these actions should, he thought, give public evidence of a determination to follow orthodox principles in defending the international exchange value of the dollar.

2. Authority to effect transactions in intermediate- and longer-term securities.

The Committee authorized the Federal Reserve Bank of New York, between this date and the next meeting of the Committee, within the terms and limitations of the directive issued at this meeting, to acquire intermediate- and/or longer-term U. S. Government securities of any maturity, or to change the holdings of such securities, in an amount not to exceed $500 million.

> Votes for this action: Messrs. Martin, Hayes, Irons, King, Mills, Mitchell, Swan, and Wayne. Votes against this action: Messrs. Allen and Robertson.

The renewal of the authorization was without indication of change in the views stated regarding it when the authority was previously renewed.

December 5, 1961

1. Authority to effect transactions in System Account.

The policy directive to the Federal Reserve Bank of New York calling for open market operations with a view to encouraging

credit expansion so as to promote fuller utilization of resources, while giving consideration to international factors, was renewed at this meeting without change.

> Votes for this action: Messrs. Martin, Hayes, Balderston, Irons, King, Mills, Mitchell, Robertson, Shepardson, Swan, Wayne, and Fulton. Votes against this action: none.

On the basis of more complete data for October than had been available at the preceding Committee meeting, together with preliminary data for November, it appeared that after a period of hesitation in August and September a strong growth trend in the economy had resumed, although without indication of excesses or undue exuberance. December production schedules, particularly in steel and automobiles, suggested a further upward movement in industrial production by year-end, and the tone of business sentiment, as reflected in district reports, was generally on the optimistic side. Additional improvement was noted in retail sales, as well as in manufacturers' sales and orders. Also, although there continued to be a substantial amount of unutilized manpower, preliminary unemployment statistics for November indicated a significant percentage reduction, for the first time in a year. Prices continued to show general stability. Despite recent improvement, there remained a degree of uncertainty regarding the probable future pace of consumer outlays, and there was likewise little evidence of an upward surge in plans for plant and equipment expenditures.

Despite the apparently accelerated pace of economic expansion in November, the rate of bank credit and deposit expansion seemed to have slackened, following the pronounced increase in September and October. Nevertheless, money markets were relatively firm in November until the end of the month, and interest rates generally rose somewhat. Treasury bill yields rose in the latter part of the month to or slightly above the peaks reached at various times of seasonal pressure during the past 15 months.

There was no evidence of improvement in the international