

Transcript of Press Briefing

held by

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Chairman, Board of Governors of the Federal Reserve System

and Senior Board Staff

at

Noon, April 22, 1974

Room 2121

Federal Reserve Building

20th Street and Constitution Avenue, N. W.

Washington, D.C.

Mr. Coyne: This will be a press briefing or press seminar, whatever you want to call it. You can quote people. The staff, however, is very shy, and if you quote any of the staff they would prefer if you just use Federal Reserve officials. If the Chairman says anything that's newsworthy you may quote him by name, but I understand he doesn't plan to do much talking. We'd like to embargo all material for 2:00 p.m. We've had a problem finding the proper time for the press briefing. We would have had it at 2:00 p.m. but there is some conflict involved, and this policy record normally goes out at 2:00 p.m. I'd appreciate it if you could limit the discussion to FOMC procedures. That covers a wide area as it is, and I am sure you'll have a lot of questions. I think you all know Dr. Burns. Seated at Dr. Burns' right is Chuck Partee, who is Managing Director for Research and Economic Policy. To my right is Steve Axilrod, who is an Adviser to the Board, in Chuck's office. And then to Chuck's right is Arthur Broida, who is an Assistant to the Board in the Research and Economic Policy field and also Secretary of the Open Market Committee. Any questions about the ground rules? Are they agreeable to everyone? Mr. Chairman.

Chairman Burns: Well, this is going to be a meeting devoted largely but not entirely to FOMC procedures, and the emphasis, I take it, will be on an extension of the factual information that we provide in our releases of the proceedings of the FOMC. These releases come as you know with a 90-day lag. I think we might start with Mr. Partee and then see where we might go from there.

Mr. Partee: Thank you, Mr. Chairman. Gentlemen, the first item in the handout that you've received this morning is the summary record of the policy actions of the FOMC. Now, I don't know whether you read this very carefully or not when it comes to you, given the 90-day lag after the actions have been taken, but I would like to point out to you that there is more here than a record of policy actions. In effect, this document distills a good deal of the information that has been considered by the Committee at its meeting. We have a procedure here for bringing together a great deal of information on the economy and on financial markets, which I am sure most of you have heard about at one time or another.

First, we have something called the Green Book, which presents statistical material that has come out since the previous meeting of the Committee. This document tries to evaluate the meaning of the statistical material, puts it into the form of a projection of the economy and of changes in the projection of the economy that may have developed as compared with a month earlier.

Secondly, we have something called a Red Book. Now the Red Book is material provided by the Federal Reserve Banks and it represents the thinking of important business people and the comments of important business people in the individual Federal Reserve districts concerning their business, concerning what they know of what has developed in the economy as they see it in the past month, and it includes, among other things, the comments of the directors of the Federal Reserve Banks. I might remind you that every Federal Reserve Bank has nine directors, every branch has five or seven. There are twelve Federal Reserve Banks and 24 branches, so that there's a pretty fair sampling

of opinion that comes to the Committee. So the Red Book reports on developments and thinking as it seems to be developing around the country.

We also have a Blue Book that we present to the Committee before each meeting. The Blue Book discusses the credit market developments and the financial developments over the preceding month or so, and the relationships between credit markets, monetary aggregates, and interest rates that have developed in the past. And finally, there is a period -- that often lasts for three or four hours -- of Committee discussion of all of this material and of other points of interest that the Presidents and the Members of the Board may have learned. And there is a discussion of how to evaluate all of this and to put it all together. That includes, for example, a presentation to the Committee by myself as the Senior Economist of the Committee, and by Steve Axilrod, developing further the questions of the Blue Book. When you put all this material together, it must make a stack of 2 or 2-1/2 inches deep for any one meeting of the Committee. I've no doubt that it's a more comprehensive look at the economy and the financial markets than is gathered together any place in the country. This is done monthly, and I think that we have quite good intelligence about what has been going on.

But I want to point out to you that there is a difficulty here, and the difficulty is that the Committee, as a necessary part of its business, needs to forecast. It needs to forecast the economy, and we try to help the Committee do that by means of the Green Book projections. It needs to forecast the financial markets and the relationships among financial markets, and we try to help the Committee do that. But forecasts are always dangerous, and they are always uncertain, and they often have degrees of error in them, and it's one of the hazardous parts of the game that we have.

And for that reason, we often think in terms of ranges, rather than specific numbers. Now, we think, usually, in these forecasts, in terms of long-run relationships. That is to say we believe that monetary policy operates with a lag in having an influence on the economy. And we believe also that the little ups and downs that occur, sometimes the bigger ups and downs that occur in financial markets, month by month, in very short time periods, don't have very much effect, basically, on the thrust of the development of the economy. But there is a problem in this, and that is that the Manager has to operate day by day in carrying out the instructions of the FOMC. He has to know what to do from one Committee meeting to another Committee meeting about a month hence. So in instructing the Manager, it's necessary to reduce these broader, longer-term considerations down to questions of what do you do here in this period immediately ahead.

We've been operating with this procedure for several years, but now the specifications that are given to the Manager are going to be shown in the policy record entry, and thus become available to the public, and this is shown on page 9 of the material before you. What we have here that didn't exist before is the sentence: "Taking account of the staff analysis the Committee concluded that growth in M_1 and M_2 over the January-February period at annual rates within ranges of tolerance of 3 to 6 and 6 to 9 per cent, respectively, would be consistent with its longer-run objectives for the monetary aggregates." And then they also specify an RPD growth rate range which had been done over the past couple of years in the public material, in this case 4-3/4 to 7-3/4 per cent. And, in addition, there is

a range through which the Federal Funds rate would be permitted to move that is specified, and in this case it was 8-3/4 to as high as 10 per cent.

So those are the changes that have been made in terms of the material that becomes available to the public and the press, still with the 90-day lag. And as I wanted to emphasize before, these are projections. They are projections of relationships. They are uncertain because of that, and often the Manager, the Chairman, and in some instances, the Committee, have some difficulty interpreting how these relationships in practice are working out, and what the Manager should do in response to them. So that's the background. Now Steve Axilrod deals with the Manager on these questions on a day-by-day basis as we proceed from one Committee meeting to the next. And so I would like to introduce Steve and ask him if he would like to talk about using these specifications as an operating matter in looking at developments in the course of the days between Committee meetings. Steve.

Mr. Axilrod: Thanks, Chuck. I'll just try to take a very few minutes of the group's time because perhaps we can, in being responsive to questions, hit some of the things that concern you about these operating procedures. Chuck has stressed the ranges and the uncertainties that surround them. I'd like to note for you the fact that we have, in the printed material we gave to you, a background paper to publication of the numerical specifications. We have attempted to explain some of the reasons for the ranges, why there may be deviations from the ranges and the role of money market conditions in our operations. What normally tends to happen

after the Committee sets its specifications at a meeting, and at this meeting the specification for M_1 was 3 to 6 per cent ...

Chairman Burns: These are annual rates.

Mr. Axilrod: Annual rates. For M_2 it was 6 to 9 per cent, and for the RPD's, Reserves Against Private Deposits, it was 4-3/4 to 7-3/4 per cent. Now the Committee uses these three ranges in part because experience has shown you cannot rely completely on any one aggregate at all times to reflect the most desirable course for the financial markets. And, secondly, because relationships among aggregates are very loose. We cannot be certain in the short run, or indeed for the long run, to what extent the public is going to use the reserves supplied by the Federal Reserve for time deposits, or to what extent they are going to use them for demand deposits. That would affect the relationship of M_1 and M_2 . It would also affect the relationship between reserves and M_1 and M_2 because time deposits require less reserves than demand deposits. At the same time, with respect to the Federal Funds rate, we cannot be absolutely certain about the strength of loan demands in the short run. If loan demands are extremely strong banks will issue large CD's, sell bills, and some banks will borrow much more in the Federal Funds market, and this will tend to put upward pressure on the Federal Funds rate. And so the range will permit some reflection of these pressures in the actual movement of market rates. So that as you follow a reserve target you get movement in the Federal Funds rate as loan demand pressures ebb and flow over the short run. In an operating sense, what we have to do then is wait to get new data for a new period. And as new data

comes in we are going to find out, as you all have seen from experience, that sometimes one week's figure on deposits will turn out to jump \$1 to \$2 billion from previous weeks. We might have expected that. We might have figured out the special reason for it. If there's a sharp drop in U. S. Government deposits, for example, then this will lead to a temporary increase in demand deposits and it won't surprise us, and we would have allowed for it in our policy.

On the other hand, we have a very complex economy and someone may have paid some money a little sooner than expected, and money demand may jump \$3 billion more than we expected. And the problem then becomes what do you do about that? Do you assume it's temporary, and take no offsetting action. Or do you assume it reflects some more permanent development, and the rise in money market rates that's in train should be accommodated. The normal thing to do under these circumstances is to monitor your continuing flow of data, that is, next week you get new data that will verify whether that increase was really there. That is, maybe next week the deposit figures will drop a billion dollars, so you will begin to sense that you had a temporary bulge, and you won't tend to be as grudging in reserve provision as otherwise.

Now when you get through with this whole process, you may find out that at the end of the period your money growth, instead of being within the range, was outside of the range. And I think the odds are that it will be outside very frequently as compared to being within. And the reason is because of these uncertainties that I've mentioned before that affect very short-run moves in deposits and reserves and in the Federal Funds rate. And what you're likely to find is M_1 may be outside the range, M_2 within the range, and RPD within the range. Or you might find RPD outside the range,

M_1 in the range, and M_2 outside the range. There could be any number of combinations like this that will develop. The Committee, of course, realizes this and it will attempt in its general discussion to give some sense of how things might evolve.

Now, as a general principle, you can't foresee every uncertainty. Otherwise it wouldn't be an uncertainty, of course. And so the Committee has provision for procedure when significant inconsistencies develop in these short-run guides -- the System Account Manager informs the Chairman immediately of this, and the Chairman then determines whether there should be a special communication with the Committee. I don't really want to take any more of your time in expanding on this. I think you'll find much of this material in these background notes that we have presented to you.

Chairman Burns: Very well, let's go to your questions, now.

Mr. Gannon: Dr. Burns, why are you making this material available at this time?

Chairman Burns: Well, you know, we keep on reviewing our procedures, and we've changed them from time to time, and we've worked in the direction of larger disclosure. And the reason that this information is being put out now, and was not put out earlier, is that the Committee had finally reached the decision to do that, after deliberating on the matter over a considerable period, studying it up and down. The Committee reached that decision, and it became effective immediately thereafter. The explanation is very simple.

Mr. Thomas: Well, could you reverse it and say what were the hangups that previously existed to putting it out.

Chairman Burns: Well, you speak of hangups. The Committee was not of one mind, really, when we finally reached this decision, and the majority swung in the direction of this greater disclosure. And you may ask why. Well, in the opinion of some Members of the Committee -- and some still feel this way -- this factual information which we at least have the illusion of understanding thoroughly, will not be understood well enough even by you men, and then understood still less perfectly by your readers. Perfectly natural, even if not entirely commendable.

Mr. Partee: If I may say so, Rich, the difficulty here is the possibility of misinterpretation. You know sometimes these numbers are going to be lower and sometimes they are going to be higher ... and the problem is that one has to be realistic. You might have a money growth rate that's a good deal higher than the Committee wishes. The two months included in the specifications include the month in which the Committee is meeting and the following month, and so if you started out on a high track in that period, the chances are you're going to have a pretty high number for the two months. Maybe higher than the Committee would desire in the long run. Or a lower number than the Committee would desire in the long run. And that's why interpretations can be difficult, I think, for the general public. We're going to try to help you to the extent we can in this record of policy action and the material that surrounds it, but we can go only so far in doing that. As I said at the outset, I'm not sure how carefully the policy record entry is read anyway by the press or anybody else.

Mr. Axilrod: Chuck, I might point out that some of the problems of interpretation in this record arise when you compare the specifications with actual developments. You will find that M_1 was right within the middle of the range in this period, it was around 4-1/2 per cent.

Chairman Burns: Don't draw any generalizations from this one experience.

Mr. Axilrod: On the other hand RPD was below the range. It was 3.3 per cent. And M_2 was above the top of the range. It was 10 per cent. People decided to put more of their savings in time deposits in this period. That's not something that we can predict extremely well. We normally can predict that a lot better than we can predict what they are going to do with their demand deposits. So the Chairman is quite right on that. And banks didn't issue CD's very much in this period, so you required less reserves to support those CD's. So I think you're going to find that a lot of variations around these ranges are going to be difficult to interpret by you and your readers.

Mr. Gannon: Are those statistics you just gave us for the months of January-February combined?

Mr. Axilrod: Yes.

Mr. Nokes: Dr. Burns, if it appears that the information might be misunderstood, what then were the reasons to go ahead and release the information?

Chairman Burns: Well, over the years the Federal Reserve System has moved in the direction of ever greater disclosure, and perhaps I ought to say a few words about that now. Our central bank publishes

vastly more information and publishes it in more timely fashion than any other central bank in the world. Now this didn't happen over night; this has evolved over the years. That is the situation today and it has been the situation for a number of years now, I believe. Second, in addition to the information that we publish regularly, we receive very numerous inquiries from Members of the Congress, and these inquiries are all answered rather fully, and as a rule quite promptly. Third, Members of the Board of Governors, particularly the Chairman, testify with considerable frequency before the Congressional Committees and answer with considerable candor questions that are put to them. And, in fact, this is the only central bank whose Governors are subjected to parliamentary inquiry. No Governor of a central bank outside of our country testifies before legislative committees. We do that -- and I personally do that with considerable frequency -- and I've made it clear to Congress that I'm available at any time and that this is with me a top priority.

Now, do we publish everything? Do we disclose everything?

Well, we come very close to doing that, but there are certain lags. Now take the document before you. There is a three-month lag normally before that document is released. Now the question is often put: why don't you, after you hold the meeting of the FOMC, put out a release or communique that will disclose in forthright fashion the decisions reached by the Committee. Well, the answer to that question is decisive. If we did that the financial sophisticates -- and there are such people in this country -- would rush to the telephone and take action in the securities market and other innocent people, less well-informed people, would learn about this action, come to understand it, days later, weeks later, when

markets will have turned. Therefore, if we made this information available promptly, we would become a highway for the enrichment of financial sophisticates. This our central bank will never do.

The information is made available three months later. Now this relates to operations at the Open Market desk. We carry on foreign currency operations at the Foreign desk, and we have an understanding with the Banking and Currency Committee of the House under which that information in global form is made available with a one-month lag. And the reason for the lag is, again, to prevent disclosure of a kind that would enable financial sophisticates to enrich themselves, probably at the expense of the rest of of the community. Actually the detailed information on all of our foreign currency operations is made available with a somewhat longer lag. The New York Bank puts out these releases once every six months, I believe. Recently there has been a quarterly report, less full than the six-month report.

Well, finally, we even have a six-year lag. A very full record is kept of every statement made by every Member of the Federal Open Market Committee, including members of the staff who participate in the meeting. Now that document may come to a hundred pages, a hundred and fifty pages, depending on the length of the meeting, and is made available with a six-year lag. Why wait six years? Well, I am not going to defend six years as against five, or as against seven, or possibly four, any more than I would rigidly defend a three-month lag in the publication of the directive, as against a four-month lag or possibly a two-month lag. But a considerable lag in the case of this longer document which is practically a verbatim report on what each individual said, a long lag is essential. You might

ask why. The FOMC is a deliberative body. As such, Members of the Committee must speak very frankly to one another, and they must give their opinions, or convey information they have about activities within the Administration, within the Congress, activities going on in foreign central banks, activities that are taking place or that are planned by foreign governments. Now these comments are made fully and they are made very frankly. If all of that were released to the general public, great embarrassment might be caused to governments, foreign central banks, possibly to Members of the Administration, possibly to Members of the Congress. We could put out such a document rather promptly. But in that case Members of the Committee would stop speaking frankly to one another, you see, and the kind of honest, complete deliberation that is essential to good judgment would simply not be forthcoming.

I've given you a long answer to the question. We've been moving more and more in the direction of fuller disclosure. Our record in this respect goes far beyond that of any central bank in the world. And practically everything that we do is disclosed eventually, but with lags designed to protect the people of this country, particularly small investors as against financial sophisticates. It is designed to promote frank, honest, thorough discussion, designed to prevent embarrassment, rocking of markets, possibly even unsettling of governments which complete disclosure of what is said at that meeting might easily cause, at times.

Mr. Weberman: Dr. Burns, just looking at the various ranges that are given here, if, say, in the various aggregates the growth over the following

four weeks was at the upper end of every one of the three numbers, the Federal Funds rate at the lower end, would that be considered not having met the objectives of the directive?

Chairman Burns: Well, that would mean that the judgments of the Committee have not been borne out by experience, and that is something that the Manager would be very alert to. He would see it coming before it actually happened. That is something that the Chairman of this Board would likewise be alert to, and something would happen between meetings.

Now I should add a word to the explanation that has already been offered by Messrs. Partee and Axilrod. The Committee has met and the directive has been agreed to and the specifications have been agreed to, voted by the Committee. Almost invariably after such a meeting I will meet with the Manager of the Desk, along with the men who are assembled here, excluding Joe Coyne, to make sure that the Manager has interpreted the directive issued to him correctly.

Next, every day, there is a conference call and members of our staff and one of the Bank Presidents, and any of the Governors who wish to do so, will participate in that conference call, and in the course of that conference call the Manager will indicate what is happening in the markets and what his plans for that day are, and what is planned. And at the beginning of the week he will indicate his general plan for the week ahead. In that fashion the Committee can follow very closely what the Desk does to make sure that its operations conform to the directive that has been issued to the Desk. And, of course, this is also a mechanism for keeping the Committee thoroughly informed about market developments, what is disclosed at the Desk is made available to all Members of the Committee who do not participate in that call, and that disclosure is made twice a day, and promptly. So, we have

a very intricate and thorough monitoring procedure. That's my point.

Mr. Partee: I was just going to say, Ben, that the particular specification you have given would be rather unlikely, because the Federal Funds rate range ordinarily is in the nature of a constraint in order to prevent the markets from being turned too much. But you add all of these other aggregates at the top end of the range, the chances are very strong that the Manager would be moving up through that Federal Funds rate range. It might not get to the top -- that would depend on the specific circumstances and discussions that would occur; but it would no doubt not be at the bottom of the range if the aggregates were all at the top.

Mr. Rossi: I wondered if we could possibly discuss the latest RPD experiment.

Chairman Burns: There has been a lessening, certainly, of enthusiasm. We expected more from the RPD experiment at the beginning than we do at the present time, and our whole procedure is now in the process of being reviewed, particularly the role of the RPD's. A Subcommittee is working on that at present. Do you want to add to my comments, Steve.

Mr. Axilrod: I think I would point out that the problems with a reserve measure relate to the relationship of that reserve measure to other monetary aggregates, and our experience has shown that there can be very diverse movements between the RPD's and M_1 and M_2 . So, we have not been able to view the RPD's in isolation from what's going on, not only in credit markets, but in reference to other aggregates against which it relates. And so the question then comes up whether other reserve measures are perhaps better. We are investigating these various problems.

Mr. Berry: At a meeting in New York on Friday, members of a panel were discussing the open market operations, and suggested that the Fed would perhaps be well advised to be in the market less than it is, perhaps limiting its actions to one or two days a week, or alternatively . . .

Chairman Burns: I'd love that. Once a week would be wonderful, once a month even. That is well-meaning, but I'm afraid a naive suggestion.

Mr. Berry: In addition to that or in place of it, persons were also suggesting that you be in the market only until noon.

Chairman Burns: Well, that, too, I'd find congenial if it were practical, but I'm going to leave that question to Mr. Axilrod. What do you think?

Mr. Axilrod: Well, normally most of our operations are undertaken around noon, or earlier, so that's normally the case. There are times when markets move a little more rapidly than had been contemplated, so we find it necessary to enter the market to accomplish our objectives. Sometimes we buy in the afternoon as a technical matter because we don't want delivery today, we want it tomorrow. We give the market fair notice by doing it in the afternoon of the preceding day. It's a purely technical matter, so I think I don't see myself any particular virtue to limiting yourself to very short hours of the day. But as I say, normally the bulk of our operations are completed in the morning because if they weren't you wouldn't have had your market impact that day.

Chairman Burns: You know, if I were a Czar, I'd have these fellows at the Desk 24 hours a day.

Mr. Partee: I might point out, John, that noon in New York is only 9:00 a.m. in San Francisco. The banks have just barely opened, and sometimes things happen out there that require an action.

Mr. Weberman: The background paper points out there is little reason to permit sharp, short-run swings in interest rates, for example, 4 or 5 percentage points over months, and such extreme swings reduce the efficiency of the financial markets function. What would be an acceptable maximum -- if 4 and 5 points is not acceptable?

Chairman Burns: Well, no. I was just about to give my colleagues some advice. Let's see what they do on their own.

Mr. Partee: Well, I would say that the normal acceptable swing that the Committee believes is acceptable is indicated by the range of tolerance on the Federal Funds rate, that is one-quarter, one-half, in that area, rather than 4 or 5. Now sometimes, when exceptional circumstances develop, the Committee may decide to broaden that range, either at its meeting or at a special telephone conference call, or in a wire. I can't recall an instance where any broadening action was ever taken getting up to 4 or 5 points. Can you Steve?

Mr. Axilrod: No. We have gone back and looked at the range of variation, and I think my memory was that maybe there was a month when the Funds rate, for example, might have moved a couple of percentage points. That statement isn't specific as to rates, but you could imagine what would happen if the long-term rate moved 5 percentage points. You'd eradicate capital values instantly.

Mr. Cohn: There have been some pretty sharp interest rate swings since this FOMC meeting. Are they disturbing? Like 150 basis points in the market.

Chairman Burns: Well, the Federal Reserve fortunately has only a tangential relationship to the stock market, and it has a still more peripheral relation to commodity markets. Markets will swing and one of the characteristics of markets is that markets will make big judgments. That is one of the characteristics of money markets. The judgment will be arrived at by participants about Federal Reserve intentions, and a slight move on our part may not only be exaggerated, but can be misinterpreted by markets. Small moves by the Federal Reserve tend to be magnified by markets. That's the way our markets function.

Mr. Cohn: Do you believe the markets have been magnifying or misleading about the Federal Reserve's intentions over the past few months?

Chairman Burns: They certainly have been magnifying.

Mr. Gannon: Do you believe they could make available . . . or the portion of that six-year period you've been dealing with in specifications . . .

Chairman Burns: Well, I cannot really predict that. We may make some historical data available, but I can't say that at the present time. Whatever we do, we'll do after due deliberation.

Mr. Partee: At this time, we won't . . .

Mr. Berry: Dr. Burns, you said there was not unanimity on the Board in deciding to make this disclosure. Is the vote recorded? Is that part of the public record?

Chairman Burns: Mr. Broida.

Mr. Broida: No, it was not a formal vote of that sort. There was a general discussion and they reached a consensus, but not all Members shared in it.

Mr. Steiger: That's a concensus? Could someone comment or explain the comment on page 9 in saying that the Committee calls for growth in the monetary aggregates, including a slightly higher rate of growth in M_1 than contemplated earlier. Does this suggest that a 3 to 6 per cent range is higher than it had been, or exactly what?

Mr. Partee: The reference there is to the longer-range rate of growth. The specification is for the short-run target, and I would think it would be fair to conclude that whatever the longer-range rate of growth the Committee desired was prior to . . .

Chairman Burns: That longer-range rate is not disclosed. There is a reference to it in qualitative form. The numbers are not given at this time.

Mr. Cohn: Can you compare the range, the short-run range of targets on this sheet to what it had been prior to this meeting?

Chairman Burns: We're not disclosing that information at the present time. The Committee decided to make this information available starting with the decision reached at the January meeting. As for earlier information, I'd cover that in responding to the historical question that was made just a moment ago.

Mr. Thomas: Dr. Burns, the mortgage bankers are in town and there are preliminary indications that disintermediation began about three or four weeks ago. Is this one of the manifestations or magnitudes of which you were speaking, where you feel the markets have overreacted?

Chairman Burns: Well, I'd rather not characterize it that way. Market interest rates have risen and they have risen very sharply, and whenever that happens there is a tendency for the inflow of funds to thrift institutions, savings banks, and the savings and loan associations to begin falling off. Some such movement to which you refer may well be getting under way. But I don't want to characterize it.

Mr. Thomas: Well, could we anticipate that the Fed would be as active as it was in the last such episode in attempting to cushion the effects? This is something which is sort of a new policy. Under your Chairmanship, the Fed took some rather strong leadership in the various housing agencies and mortgage financing agencies in the Government and a few measures of its own.

Chairman Burns: Well, we submitted a report to the Congress in March 1972 on instability of the housing industry, instability of mortgage finance, and how greater stability might be achieved. That report was based on a very thorough study conducted by our staff with the aid of a rather large number of outside consultants. I would have hoped that the Congress, being so deeply concerned about the housing problem, and having been so deeply concerned over the years, would consider the recommendations of that report and in due course I am sure the Congress will. Because even if our recommendations are turned down, in the process of evaluating our recommendations perhaps wiser counsel will be given to Congress.

This is a problem that we've lived with for a very long time. Whenever market interest rates rise, or thrift institutions begin to experience difficulty, the whole building industry undergoes a downward fluctuation. It's an old problem. It's not unique to this country. It's found in every country practicing free enterprise, and interestingly enough, instability of the home building industry is found also in the socialist countries. No good solution has ever been worked out. We took a stab at it, and I think we made a very serious study, and we have made some very worthwhile recommendations. I hope that before long the Congress will study our recommendations and improve on them.

Mr. Gannon: Dr. Burns, a recovery in the housing sector is counted upon as being one of the underpinnings of a general second-half economic recovery. In recent days I have heard some economists begin to worry out loud about whether a policy on the part of the Fed permitting high interest rates would kill off that recovery in housing and perhaps endanger the recovery itself. Would you have some comment?

Chairman Burns: Well, I think, to the extent that disintermediation sets in, whether that happens because of what the Federal Reserve does, or whether it happens in spite of what the Federal Reserve does, the outlook for housing will deteriorate. Now there are devices other than those within the control of the Federal Reserve System for dealing with problems in the home building industry. And if, let us say, the Federal Reserve System is carrying out a policy of limiting the rate of growth of the money supply and bank credit, and if that should, in and of itself, release forces that are detrimental to the home building industry, these negative influences could be offset by actions taken by the Administration, or by actions taken by

the Congress. The fortunes of the home building industry do not depend exclusively, or even preponderantly, on what is done by the Federal Reserve. And certainly to shape monetary policy with an eye to the fortunes of the home building industry and neglect the rest of the economy, and in particular to neglect the great and very dangerous problem of inflation that this country faces, would be extremely unwise. There are other ways of encouraging home building. And ways that would not involve a serious cost, or serious losses to the rest of the economy.

Mr. Partee: May I just comment on that, too, Jim. We have attached here a chart and a table showing changes in M_1 and M_2 and you will note that over recent months even the trend line for the 6-month rate of growth has been moving up. It went up considerably for M_1 and has been moving up somewhat for M_2 . We could have had a chart on M_3 but it would have shown relative strength also. So that the rise in interest rates that occurred in the last couple of months isn't because there is no money and credit being supplied to the economy -- it's because the demands have been very, very strong for money and credit in the economy. It tends to raise some question about the basic premise that you gave at the beginning of your question that housing was going to account for the recovery. There is not only housing, but there are many other sources of demand for credit that are very strong at this time.

Chairman Burns: Let me just say another word. We're having a veritable explosion in business loans, and our monetary aggregates, if anything, have been growing too rapidly. And I am not letting out any secret when I say that they have been growing faster than the Federal Reserve wished or intended. The demand for credit of all sorts has been extraordinarily large, extraordinarily rapid. Now as to the expectations of

recovery, there are numerous reasons why some economists, many economists, expect a recovery to take place in the second half of the year. But I think Mr. Gannon was right in saying that one of these reasons that economists broadly have been counting on is a recovery in home building. And he is also right in suggesting that to the extent that interest rates rise, and to the extent that mortgage credit becomes less readily available, this, in and of itself, will be a negative influence for home building. There is no escape from that. But bear in mind what I said. There are other ways that could be used by Government outside of the Federal Reserve System for encouraging home building.

Mr. Weberman: Let me ask a technical question on Federal Funds. People at the Federal Reserve have often spoken of the very broad range. The market sees what they call trigger points, intervention points that are about half a per cent apart when reserves are put into the banking system or taken out. How do we reconcile that with the per cent range that's given here.

Chairman Burns: I don't know where these half per cent trigger points come from -- you've raised a point that I'm not aware of, but let our expert answer this.

Mr. Axilrod: Well, this range refers to the weekly average Federal Funds rate, and if you were moving up in a range here, for example, you might start out at 8-3/4 and he might have ended the period at 10. That wasn't what developed in that period, but that's an example. In the week

where he was starting out with providing reserves that he thought would produce a funds rate somewhere around 8-3/4, there would be days the Federal Funds rate would tend to go up and days when the funds rate would tend to go down. So on any day he can't be very certain about his reserve factor projections. So, when the rate tends to go up, he'll think well maybe I've got a wrong estimate of the factors affecting reserves and he'll put in some reserves to allow for that wrong estimate. And if it tends to go down, he'll say that the estimate is wrong in the other way, and when this happens the market will say to itself, my gosh, he's putting in reserves at this funds rate and another day later it will end up he's taking it out at that funds rate and on Wednesday it turns out he doesn't do anything and the rate might go to zero or go up to 15 or 20 per cent. But all they are seeing is his gauging the reserve conditions partly by using the funds rate as the measure.

Mr. Partee: I might say, Ben, that on the spec sheet, item 4 says the Federal Funds rate is to be moved in an orderly way within the range of toleration. Now I'm not saying there's anything magical about a half, but you might not think that you were using the whole 1-1/4 point range from day to day and going up and going down. It's a four or five week interval we're talking about.

Mr. Axilrod: I might also add that these averages hide a lot. There are days when you will have trading as low as zero and as high as 10 or 12, let's say a Wednesday, or in an ordinary day the range of trading might be pretty wide but small amounts of trading will occur at low rates, small amounts of trading at high rates, and the bulk of the trades in and around the average.

Mr. Steiger: In view of your earlier comments, Dr. Burns, about the explosion of business loans, I take it that you would not support the suggestion from some Members of Congress that we should have a tax cut.

Chairman Burns: I do not.

Mr. Weberman: On the business loan question, have you been suggesting to bankers that they somehow cut down on the amount of loans they are making?

Chairman Burns: Oh, I have not issued any admonition to the bankers. However, I think bankers pretty well know what I think. This country is facing, as I said more than once, and I'll continue to say it and act accordingly, it's facing a very dangerous problem of inflation, and excessively rapid expansion of bank loans is a deep matter of concern to me and to the System, and excessively rapid rates of growth of all monetary aggregates are. We are not going to get this inflation under control if that continues, and if we don't this country is going to be in very great difficulty. We as a System will continue to conduct ourselves in such fashion that the supply of money and the supply of credit may continue to expand, but only at a moderate rate. And needless to say, we will always respect our obligation of being a lender of last resort. And there need be no fear of a credit crunch or liquidity crisis, for we are not going to sit back and prepare a monetary path to the continuance of rapid inflation. On the contrary, we hope to do our part in subduing it. And let there be no mistaking our determination to do this.