

Consumer Credit Management Program  
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CENTRAL BANKING POLICY AND ITS RELATION TO CONSUMER CREDIT

My lecture today is entitled either "Central Banking and Consumer Credit" or "Consumer Credit and Central Banking". In either case the emphasis is placed far more on central banking than on consumer credit. There are really two reasons for this emphasis. First, you have heard a great deal over the past few days about various aspects of consumer credit - what it is, how large it is, how to administer it in advances and collections, what forms it has taken and may take in the future, and so on. It would be sheer waste of your time and great presumption on my part to attempt to recover this ground and hence whatever I say on these aspects of consumer credit will be minimal and no more than necessary to underline the points I want to make about consumer credit and central banking. The second, and perhaps more pertinent reason, is that Professor Chapman asked me to place the emphasis on central banking and since I am a central banker it comes very natural to me to do just this.

It will be useful, however, to give you briefly some definitions and numbers concerning consumer credit as I will use the term so that you will know what I am talking about when I do refer to consumer credit. As I use the term, it refers to credit which finances the purchase of consumer goods and services, except housing. Thus it includes not only what many people regard as consumer credit and what is pertinent when we talk about consumer credit control - instalment loans which are used mainly to finance the purchase of consumer durables, and those either secured by the goods itself or those made on other security such as small personal loans - but also charge accounts or convenience credits which finance at short term mainly nondurables and services, and single payment loans, including those on life insurance.

The statistics on consumer credit are pretty good but not perfect by any means. Some fifteen years ago I headed a small Federal Reserve technical committee which attempted to put together an improved series on consumer credit and I think did a fairly good job. We had the valuable aid of a number of outside consultants, both from the consumer credit trade itself and from the universities. There have been numerous additional revisions of the data and at present they are, as I say, pretty good. Direct instalment credit data are quite good. One major difficulty is the obvious one of attempting to classify purpose of loan when there is not much objective data to go on. Thus the purpose of a small loan or a life insurance loan is somewhat obscure. Also, one can argue that a lot of charge account credit really is not credit at all except in a very technical sense - although it seems to me that there is no question about some of it being real credit, especially if times get bad. We see this kind of development in my area especially in the mining regions.

In any event, leaving aside those fairly obvious imperfections, we have a reasonably accurate time series on consumer credit extended, repaid and outstanding. At the end of 1962, using my definitions, the volume outstanding was about \$63 billion, of which \$48 billion represented instalment credit and \$15 billion noninstalment credit. Taken as a total this represented about one-seventh of personal income.

As another way of looking at consumer credit, in 1962 the total of net funds raised by nonfinancial borrowers was about \$58 billion, with private sector borrowers raising about \$49 billion. Of this sum about \$15 billion was in the form of loans of which a little more than a third - about \$5-1/2 billion went to consumers. Note that these numbers all represent net increases; total or gross extensions were, of course, larger. Just for comparison, mortgage debt increased by a net of \$24 billion, of which mortgages on 1 to 4 family dwellings alone rose almost \$16 billion. Total mortgage debt outstanding at the close of 1962 was \$250 billion. So while consumer credit, as I define it,

is big business, it is dwarfed by mortgage credit.

Well, so much for definition and numbers. Now I turn to central banking. We shall return to consumer credit and its interest to central banking at a later point in this lecture.

Virtually every country in the world has a central bank. The oldest of these banks is the Bank of England which goes back more than 250 years. The primary reason for the existence of central banks is that money will not manage itself. As the Federal Reserve Bank of Philadelphia puts it in a booklet on the subject - "Money: Master or Servant?"

The central bank of the United States is the Federal Reserve System which will be 50 years old this winter, if you date its beginning from the signing of the Federal Reserve Act by President Wilson in December 1913, or 50 years old next fall, if you date it from the actual opening of the Reserve Banks in November 1914. Thus we have a fairly young central bank in this country.

Actually we had tried central banking in this country twice before the founding of the Federal Reserve System; first, immediately after the birth of the Republic in 1791 when the First Bank of the United States was chartered for 20 years. Its charter ran out in 1811 and was not renewed. It had done little. In 1817 the Second Bank of the United States was chartered, also for 20 years. In general it performed fairly well but it got badly mixed up in politics and became a major political issue so that in the Jackson Administration it was at great odds with the government and its charter was not renewed either. Then for 75 years we had no full scale central bank, although a combination of the Treasury and the big commercial and investment banks performed some essential central banking functions.

The recurrent financial panics of this period, culminating in that of 1907, led to a major study of the financial system of the United States and resulted in the establishment of the Federal Reserve System. In a very real

sense it can be said that the United States decided after 75 years of experiment that it preferred money to be the servant rather than the master.

The primary reason for dissatisfaction with the money and credit system that existed prior to the establishment of the Federal Reserve was its lack of elasticity. Commercial banks can, of course, create money through their credit expansion activities - extension of loans or purchases of securities. They can do this simply because they give a book credit, a deposit, to the borrower or the seller of a security. They can do this indefinitely and without limit as long as no one asks for currency. When currency, or gold, is taken out of the banks it causes a break in the deposit creation process. Banks know this and, therefore, even without any legal regulation there would be a sort of self-imposed automatic limit on credit expansion by banks.

Banks also know that asset values change and that some assets are very liquid and some are very illiquid. They have found from bitter experience that forced sale of even very good assets produces violent value shrinkage. This also acts as a limit on credit expansion.

Now if banks could print their own money and people were willing to accept it in payment, there would be no problem in providing asset liquidity or in providing for continuous credit expansion. In early America, banks did just this and people were willing to accept their bank notes because they thought they were good. The test of goodness then was redeemability in gold. But a lot of banks were over-enthusiastic about note issue and a lot of bank notes turned out to be irredeemable and not very good. So partly to protect people who took bank notes and partly because our government believed that note issue was really more government than private business, the National Bank Act in 1863 confined the note issue privilege to national banks and allowed them to issue notes only equal to the amount of government bonds which they held. In effect, this made government bonds, and hence the government itself, the backing for national bank notes.

This process did not provide for an elastic currency even though it did provide for a safe one. Unless government debt increased, the note issue could not increase. And with government debt being paid off after the Civil War the note issue actually was subject to contraction. Other currency backing, gold or silver, or circulation of metallic money would have helped if there had been enough but there was not. Many of you have read Bryan's "Cross of Gold" speech and know of the movement to value silver at 16 to 1 with gold. This really reflected in large part the nation's need for more money supply.

The kind of system we had then provided for a sound currency but an inelastic one, a credit expansion system that was self-limiting because of fear of asset illiquidity, and no real way to avoid these difficulties. There were almost always seasonal shortages of credit and of money. There were at times financial panics and forced asset liquidation. And, as noted, the great financial panic of 1907 led to a thorough study by a National Monetary Commission which resulted in the Federal Reserve System.

The Reserve banks were given the power to issue currency backed by commercial paper. Since these banks were really official institutions, the currency was acceptable - and redeemable, since we were then and would continue for the next 20 years on a full gold standard. It would expand as the economy's needs expanded because the loans made by the banking system would be discountable at the Reserve banks and then used to back additional note issue. When the economy needed less credit, there would be less discounting, less paper available for currency backing and hence the currency would be elastic. Seasonal needs could be met easily and panics avoided. There would need be no forced asset liquidation because the central bank with note issue power could make the assets liquid and people would accept the currency.

Well, the System turned out to be somewhat less perfect than many of its supporters had hoped. It was, however, a great improvement on the former

set-up because it did provide the elastic currency. It did not, however, until 1935 has sufficient power to provide full asset liquidity. It now has such power.

Now I want you to note one important point here. The Federal Reserve provided a managed money system even under the gold standard of the teens and the 20's just as every central bank the world over has provided. And the System itself had to maintain a gold reserve, partly to redeem notes if there was demand for such. It still has to maintain a gold reserve under the law, so its expansion powers also are limited although not seriously.

But this ability to expand money and credit, while a boon to the economy, brought new problems with it. There was always pressure to expand and always resistance to contraction. And yet while a money and credit system should grow in keeping with the needs of the economy, it should not grow too fast for the economy to absorb. And created money itself could not do the job that real resources had to do. And to explain this I now want to turn to give you a brief course in monetary theory.

I begin with the often-maligned Quantity Theory of Money which in its simplest form is expressed by the equation of exchange,  $MV = PT$ ; where M equals the volume of money, V equals its velocity or rate of turnover, P equals the price level and T equals the volume of trade or business in physical terms. The equation says that the volume of money multiplied by its turnover rate equals the physical volume of trade multiplied by its price level, and in a sense is a truism at any given point in time.

Now every central banker is at least a partial, or perhaps I should say a practical member of the Quantity Theory School. But there are few, if any, central bankers who can be classed as full-fledged quantity theorists. The theory has undergone many refinements since it was first put forth in the simple equation I gave you, but it still rests basically on not only the

equation of exchange but on a belief that there is a direct and unvarying relationship between the volume of money and the price level. In essence, the pure quantity theorist says that in the equation  $MV = PT$  both  $V$  and  $T$  change slowly and therefore that the dynamic factors are  $M$  and  $P$ . If  $M$ , the volume of money, increases too fast,  $P$  will have to increase proportionately and there will be price inflation. If  $M$  does not increase fast enough,  $P$  will fall and there will be deflation. There has been a great deal of effort expended to prove this theory statistically. Its principal prophet in this country is Professor Milton Friedman of the University of Chicago which is the foremost university devoted to this theory. After years of study Friedman concludes that the volume of money should increase at a fairly constant rate of 4 per cent per year so as to keep the volume of money consonant with an expanding economy operating without either inflation or deflation.

Practicing central bankers part company with pure quantity theorists on two crucial points. First, they do not see the direct and unvarying relationship between money and prices. They see the velocity factor changing more rapidly and they see various interactions of the four factors, with prices affecting trade volume and vice versa, trade volume influencing money volume and money volume influencing velocity as well as prices, and so on. Second, and more importantly, however, they see the course of the economy as being determined by many factors other than money volume and believe that a constant rate of money volume increase would at times be inflationary, at times deflationary, and relatively infrequently would be neutral.

As a matter of fact, no practicing central banker has yet found a single theory of money that explains the behavior of money and interest rates under all conditions. Some theories stress demand and supply of loanable funds, some stress liquidity and velocity, some stress saving and investment, and, as

noted, the quantity theory stresses money volume. The plain fact is that the record shows that elements of all of these theories are valid under certain conditions and at certain times in the economic cycle. The trouble is that they are not all valid at any time, nor is any one always valid. So central bankers, being pragmatic people, attempt to look at all factors in the current picture when they determine monetary policy.

Now let me finish this brief excursion into monetary theory. A central banking theory of money is fairly simple and as you will see rests on the general tendencies underlying the quantity theory but stops far short of that theory's conclusions. When an economy is operating at full throttle any resources devoted to investment have to be withheld from consumption simply because at any given point in time resources are limited. Since this is so, investment has to be financed by real saving; that is, someone has to forego current consumption in order to provide the resources for investment. It follows then that increasing the supply of money under such conditions will not add to real resources but will merely be expressed in a price rise of the resources available. Created money, which is the product of a central bank, then cannot be more than a short run substitute for real saving. It can bridge temporary imbalances between current saving and the demand for investment funds, it can serve to put funds quickly and easily into the hands of those who can use them economically. And since a growing economy needs a growing stock of money, a central bank can provide for this need.

But since the economy does not always operate at full throttle, a constant increase in money volume is not desirable. During the past 60 years the American economy has expanded as much as 20 per cent in a year, in real terms, or contracted as much as 15 per cent. On the average it has grown about 3 per cent per year but very few years have been average years. Last year, in real terms growth was better than 5 per cent; this year the guess is that it will



be 4 per cent, but it might be 2 per cent or 6 per cent. What central bankers try to do is to keep watching the economy as closely as they can so as to keep the volume of money in keeping with the needs of the economy - not too much nor too little.

Now let me leave the field of monetary theory to talk for a bit about the functions and structures of a central bank. In the course of the past several years I have had the opportunity to visit and observe the work of a number of central banks: four in Latin America (Mexico, Guatemala, Honduras, and El Salvador), five in Asia (Japan, China, the Philippines, Thailand, and India), and five in Europe (England, Italy, Greece, Spain and Portugal). In general, central banks have these functions: banker for the government, lender of last resort to the financial system, supplier of currency and clearer of checks, supervisor of the banking and financial system, provider of economic intelligence and the all-important function of regulation of the volume of money and credit. Some central banks are more deeply involved in overall economic policy formulation than are others, some do direct lending to private business just like a commercial bank, some handle the country's foreign trade affairs, some do the debt management job. The Reserve Bank of India supplies directly much of the farm credit for Indian agriculture; telephone users in Honduras pay their bills to the Central Bank of that country. But while there are differences in scope of work and in manner of operation, every central bank that really is one has the key functions of money creating power and credit control power. This is the heart of a central bank and when we talk of central banking policy, this is what we are talking about.

In the United States the Federal Reserve System is the central bank. It is organized somewhat differently than most other central banks in that it is a rather unique blend of an organization structured like a private concern but with a public purpose, regional in concept but with centralized policy making.

When the Federal Reserve System was established it was believed that it should be organized outside of government so as to be independent of day to day politics and not a part of any one administration. At the same time, since its primary purpose was a public one it was made responsible to the Congress. Its employees are not under civil service, the government does not own the stock of the Banks and the members of the Board of Governors, while appointed by the President and confirmed by the Senate, have long terms and cannot be removed when administrations change. Still the System must be viewed as a public institution for its function is a governmental function and its stockholders have virtually none of the rights of ordinary stockholders. They receive fixed dividends, which represent only a fraction of System earnings, and for all practical purposes the rest of the net earnings go to the Treasury. Allan Sproul, former president of the New York Bank, put the System's position in the best way I know of - he said the System should be regarded as independent within government.

Because the United States is a big country with some rather striking regional differences, the System was organized along regional lines with twelve Federal Reserve Banks each headed by a president. These twelve presidents plus the seven members of the Board of Governors in effect form the policy-making body of the System. This body meets between 20 to 25 times a year to determine monetary policy. Of the three great credit policy instruments, the Board of Governors has statutory authority for reserve requirements, the Reserve Banks for discount rates and administration, and the Federal Open Market Committee, composed of Board members and presidents, for purchases and sales of securities. As a practical matter, there is constant consultation between the 19 men, presidents and Board members, about all of these instruments since they are mutually useful and used.

Now I hope you will have noted that I have tried to make two basic points in this discussion of monetary theory, the functions of central banks and the organization of the Federal Reserve System. The first point is that there is nothing precise about monetary policy - it is not a science, it is an art. Despite what some monetary theorists argue, there is no infallible recipe for good monetary policy except hard study and the application of informed judgment. Therefore, policy changes gradually and not abruptly and attempts to make reasonably fine adjustments. The second point is that this art is performed by mere men, men who work hard at it, are served by a first rate staff (our research organization is perhaps the best in the world), and formulate policy on a continuous basis, appraising the performance of the economy as best they can, conferring frequently and recognizing fully both their responsibilities and their imperfections. The regional structure of the System is a source of great strength; it may be said that a national credit policy is formulated with due awareness of regional differences. There is no narrow regionalism but there is knowledge of regional conditions and awareness that national averages can sometimes mislead.

I mentioned earlier the three major policy instruments of the Federal Reserve: reserve requirements, discounting, and open market operations. I do not propose to go into a highly technical explanation of the use of these instruments, but some comment on them will be useful.

In this country banks have to maintain certain legal reserves expressed as a per cent of deposits. Under such a system changing the ratio, the percentage, of reserves relative to deposits either provides for more potential credit expansion or less. Obviously with a reserve ratio of 10 per cent banks can expand credit and hence deposits by 10 times their reserves; if the ratio is 5 per cent the expansion factor is 20; if the ratio is 15 per cent the expansion factor is about 7. So the reserve ratio affects the ability of the banking system to

expand credit and the money supply. The Federal Reserve has the power, within limits, to vary the ratio and hence either permit more credit expansion or cause credit to contract.

When the System buys securities in the open market it adds to bank reserves; when it sells it subtracts from them. When the System raises the discount rate it makes the cost of borrowed reserves higher; when it lowers the rate it cheapens the cost. Thus both open market operations and discounting affect the volume and the costs of reserves available to the banking system, while the reserve ratio affects the work that a given volume of reserves will perform. All three instruments are complementary and supplementary and are used as such, but in general reserve ratio changes are made infrequently, discount rates are not changed very often, and open market operatives are used as the day-to-day adjustment mechanism.

When the Federal Open Market Committee meets, as it will on Tuesday next, all 12 presidents and 7 Board members will be there. The basic decision to be made by this body is whether to add to reserves, subtract from them, or keep them about in the same volume, and that decision will be carried out usually via purchases or sales of government securities in the open market at market prices. The Open Market Committee will discuss both discount rates and volume and reserve requirements but, as noted, actions in these fields by statute are reserved to the banks and to the Board.

The decision of the Open Market Committee may be viewed as making money and credit easier, tighter, or kept about the same. As I mentioned earlier, the normal decision would lead at most to a "slightly" easier or "slightly" tighter position if there were to be any change. Rarely are changes in policy abrupt, they are gradual; they can, of course, be cumulative or they can be offsetting from one Open Market meeting to another.

It is highly important that you recognize one key fact about these three instruments of credit policy. They are general credit control powers. They affect the total ability of the banking system to expand credit and money but they do not control in any way the particulars of credit expansion. Thus with a given volume of reserves the banks can make any given amount of loans of any type they find desirable, or buy any kinds of securities they want or have any mixture of loans and securities they want (subject of course to whatever the laws and the banking supervisors permit in terms of types of loans and securities and interest rates charged). The decisions with respect to where credit flows then are, in essence, left to the market and the millions of borrowers and thousands of lenders who operate there. In a broad sense, it may be said that by using the general credit control instruments the central bank sets the over-all limits to credit expansion or provides the general climate in which credit expansion takes place.

Now I can come back for a bit to consumer credit - which is merely one kind of credit. Should there be, as there has been in the past, a special control for consumer credit, it would be a "qualitative" control as contrasted with the general or "quantitative" controls I have noted. The only qualitative control presently possessed by the System is the power to vary margin requirements on loans secured by listed securities. This power directly influences the amount of credit that can flow into that particular use. The wartime measures of consumer credit and real estate credit control were similar in that they directly influenced the flow of credit in those fields.

There is a considerable body of opinion that holds that the general credit controls are either too effective or not effective enough and that the best way to operate credit control is through qualitative measures, either alone or supplementing the quantitative measures. The argument runs as follows: when credit in total is expanding too fast it may be that it reflects only over-much

expansion in one or two areas. If that is so, measures to hold back the total expansion will bring too much hardship to the noninflationary areas merely to curb the inflationary ones. Or conversely, if the monetary authority does not wish to cause hardship in the noninflationary areas it will not take strong enough action because it knows that only such strong action will curb the inflationary areas and that would hurt the other areas. Obviously, then runs the argument, it would be better to use specialized or "qualitative" measures which would go directly to the heart of the problem.

Well, if this is the case, why not use a whole battery of selective devices; why single out stock market credit, consumer credit, and real estate credit. Here three other points are brought out. First, these areas have been very volatile areas; credit expands and contracts very rapidly in them. Second, they are areas where credit practices have been subject to abuse; witness the stock market crashes, mortgage market collapses, and the race for easier terms in the consumer credit field. Third, these areas lend themselves better than most credit areas to relatively simple credit controls. Purposes of loans are fairly clear cut and it is possible to do a control job with minimal leakage.

So runs the argument for the selective credit instruments and particularly those for stock market, consumer and real estate credit. With respect to consumer credit itself there are these other points. Some students contend that consumer credit, left to itself, operates as a pro rather than a contra cyclical force. Thus just when everything is expanding, consumer credit expands even more rapidly and accentuates inflationary forces. When things in general are contracting, consumer credit contracts even faster, thus accentuating deflationary forces. It would be far more desirable to curb consumer credit in expansionary times so as not to get buyers of consumer durables over-bought and then see demand shrink in bad times just when it should be strengthened.

While this case comes very far from being proven, there seems to be something to it. There is no real question but that consumer credit has been a powerful stimulus to the buying of consumer durables and thus a powerful stimulus both to economic growth and to rising living standards. As such it certainly has contributed to this nation's prosperity, at least in prosperous years. But there is question as to whether it has over-stimulated consumer durables buying in the good years and thus taken away some demand that might better have come in the leaner years. As I say, this case is far from proven but there seems to be something to it.

The foregoing argument is, of course, all pro consumer credit control. The counter-argument runs as follows: the presumed fact that consumer credit is feasible to control qualitatively does not automatically mean that it is desirable to use such a control. In essence, use of such a qualitative device rests on the belief that the market forces do a less perfect job of directing the flow of credit to the various fields than would an administrative body. Economic history does not bear out this belief - at least not sufficiently to regard it as true. We do, of course, not let the market run entirely free under our - or any other - form of economic life. We shelter some markets, we impose certain rules, we interfere in some degree even in so-called free markets. But this is a question of degree and, in general, the more specific we get with market interferences the less efficient the economic function seems to be performed.

Also, it might be noted that Federal Reserve experience with consumer credit control - even in wartime when all the advantages were with the administration - was not such as to conclusively demonstrate that it was easy to administer. The idea that it is easy to administer is not held by anyone who had anything to do with the work.

Finally, I think experience has demonstrated that consumer credit does not run as free from general credit control as some have supposed and consequently

that it is neither true that credit policy has to be far too stringent for other fields to have force in restricting growth in consumer credit nor that consumer credit can expand with perfect freedom when other credit forms are being restricted.

I sum up the pros and cons on consumer credit control about like this. There may be times, particularly wartimes or very violent change times, when such a qualitative control would be not only desirable but necessary. Thus it probably would be useful to have, on a standby basis, the power to control consumer credit in the arsenal of central bank powers. My own opinion - and I do not represent myself as expressing Federal Reserve opinion - is that this is about as far as I would go in using this power. This view seems to be shared by the Commission on Money and Credit in its recent report. And I should say in concluding comment on this subject that no one I know in central banking would favor consumer credit control as a trade practice control. Some people seem to think it would be desirable to protect the grantors of consumer credit from themselves - from competitive forces. This I would oppose completely.

I now come to the concluding portion of this lecture. I have tried to cover something of the organization, structure and operations of central banking; give you a short course in monetary theory to explain why central banks exist and discuss the special aspects of consumer credit against the general background of over-all credit policy. I now want to look briefly at the recent record of central banking in this country so you can form some judgments as to the quality of its work.

The objectives of monetary policy may be expressed about as follows: it is the purpose of the Federal Reserve System to regulate the supply, cost, and availability of bank reserves with a view to influencing the supply, cost, and availability of money and credit so as to contribute to economic growth and high employment under conditions of stable values. To accomplish this purpose

the System at times has added to reserves at a rapid rate and at times at



slower rates. This has led to fluctuations in the volume and the cost of credit. On the whole, I believe an objective appraisal of System policy during the past 15 years has to conclude that it has been reasonably well conceived, well timed and effective.

I said earlier that monetary policy-making is not an exact science but an art, and that it is an art practiced by men. Since this is so, there have been mistakes made in the past 15 years. In my view the errors have been more on the side of being too easy than of being too restrictive, and I think the largest error occurred in 1954 and 1955 when the System waited too long to take restrictive action and thus contributed too much to the inflationary upsurge of 1956 and 1957. Then when action had to be taken it had to be stronger than was desirable.

On the other hand, System reaction to weakness in the economy has been, virtually without exception, prompt and effective. Policy has eased, rates have fallen and response has been good. Thus in 1953, 1957, and 1960 policy eased quickly as recession came. I certainly would not claim credit for the System completely in the mildness and shortness of the postwar recessions, but I think some of the credit is due it. And while I make this point I should make one other more general one. Monetary policy is not a panacea for economic illness. It is an important economic force, but there are many other forces operating. Probably good monetary policy alone cannot insure growth, high employment and stable values, but almost certainly bad monetary policy can make it exceedingly difficult to attain these goals.

Here I think the record of economic achievement throughout the world in the postwar period is worthy of note. A great deal has been made recently of the excellent economic performance of Western Europe and the relatively low growth rate of the United States, especially since 1957. Two points should be noted about this. First, if you run the figures back to the immediate prewar

year of 1938 and then apply a period analysis to the records of economic growth, you find that the U.S. and Canada had very high growth rates for the first decade while Europe was going backwards. This is quite simple to explain. We were the arsenals of democracy and suffered virtually no physical devastation from war. Europe was the scene of the war. In the next decade - to 1957 - Europe grew quite rapidly as she rebuilt the war's ruin - with our help. We did not have to rebuild but we kept growing as we had to meet the deferred demands of the war years and make up for those of the prewar depression. By 1957 we had done both of these, and since then our growth rate has been smaller. Europe still has great deferred demand to meet. Actually the record for the 25 years since 1938, taken as a whole, indicates as much or more over-all growth in the U.S. and Canada as in Western Europe and Japan.

Now I do not mean to imply by this that our current relatively low growth rate is good, nor that the past record should make us complacent. We have too many unused resources to be complacent - particularly about our unemployment. But I think we have done reasonably well and this should be recognized. Last year, as a matter of fact, we did better than virtually every European country in terms of growth in Gross National Product.

The second point is even more striking. I do not know of a single case in Western Europe, or elsewhere for that matter, except for some special instances, where growth has not been better in the countries which were following strong stabilization policies - both monetary and fiscal - than those which failed to do so. I have just returned from Spain. Spain, a neutral during the war, had a good growth rate. It tapered off in the 1950's and Spain began to experience inflation and lost most of its international reserves. In 1959 and 1960 Spain began to follow more orthodox money and fiscal policies. Its reserves have increased ten-fold, it has grown strongly and many people believe

it is on the threshold of an economic breakthrough like Italy. France grew more slowly and experienced price inflation until the DeGaulle stabilization program of 1959. Now it is as strong as any nation in Europe. That record runs for Germany, Italy, the Netherlands, and so on. Faster growth with stabilization and relatively firm prices, slower growth with price inflation.

The exceptions to this record are few and are special cases where for one reason or another the profligate policies have not led to actual bankruptcy because someone has bailed them out. Brazil and some other Latin American countries are object cases in point here.

Again I do not claim that monetary policy - well executed - is solely responsible for this record, but I find it difficult to avoid associating good policy with growth on the basis of the record and even more difficult to associate inflation with growth.

Now just one last word about current monetary policy. During the past few years we have faced a different mix of economic problems in this country than we had faced before. We had the slower growth rate I have noted with relatively high unemployment. Normally that would call for easy monetary policy. But we also have had a balance of payments problem which calls for reducing costs or at least keeping them from rising, and also for interest rates high enough to be competitive and attract funds. This calls for a tighter monetary policy. What we have tried to do, and on the whole have done reasonably well is to try to keep money and credit freely available without reducing its cost too much - especially on short term money. This has required a different mix of policy measures than we had used before - more frequent reserve requirement changes, less frequent discount rate moves, more buying of long term securities, and less of short term, reciprocal arrangements with other central banks, and so on. Our goals are still the same - growth, high employment and stability, but we have added emphasis on balance of payments effects.

**Conclusion - Current policy posture**

**Understand there has been comment on December change**

**Split 7 - 5**

**Change was gradual - hard to perceive in figures**

**but has been satisfactory**

**What does future hold - change.**

# D A T A

F.R. discount rate 3% August 1960		Federal Debt	\$303 billion
Required reserves	\$19.5 billion	Market	258
Excess	.6	Bills	49
Borrowed	.3	C/I	22
Free	.3	Notes	53
F.R. Securities	31.0 "	Bonds	80
		Conv. Bds.	3.5
		Nonmarket	50
		Spec.	42 "
All Comm. Banks	Loans		
	Govts.		
	Other Sec.		
	Total		
	Dep.		
		M	\$148 billion
		Currency	31 "
		Dem. Dep.	117 "
		Time	97 "

	<u>1941</u>	<u>1962</u>		
G.N.P.	126	554		
P.I.	96	441		
Disp. Inc.	-	383		
Cons. Exp.	82	357		
Dur.	10	48		
			Mortgage debt	
			1962	250
			1961	225.5
				+ 24.5

## CONSUMER CREDIT OUTSTANDING

	<u>Total</u>	<u>Inst.</u>	<u>Auto</u>	<u>Other</u>	<u>R/M</u>	<u>Pers.</u>	<u>Noninst.</u>	<u>Single</u>	<u>Chge.</u>	<u>Serv.</u>
1941	7.2	6.1	2.5	1.9	.4	1.3	3.1	.9	1.6	.6
1961	57.7	43.5	17.2	11.9	3.2	11.3	14.2	5.1	5.3	3.7
1962	63.5	48.2	19.4	12.9	3.3	12.7	15.2	5.6	5.6	4.0
Chge.	+5.8	+4.7	+2.2	+1.0	+0.1	+1.4	+1.0	+0.5	+0.3	+0.3

	<u>Total</u>	<u>Bks.</u>	<u>Sales Fin.</u>	<u>C.U.</u>	<u>Cons.Fin.</u>	<u>Other Fin.</u>	<u>Dept.St.</u>	<u>F.&amp; App.</u>	<u>Other</u>
Inst. Debt held	48.2	18.9	12.2	5.0	4.1	1.6	3.0	1.4	2.1