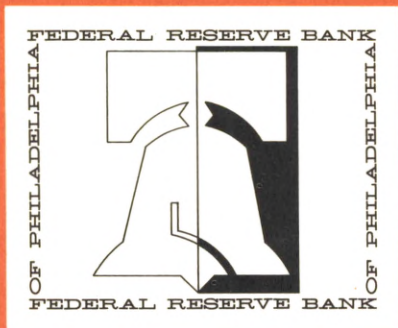


# BUSINESS REVIEW



**January 1969**

**annual report issue**

Monetary Policy, Debt Management, and Even Keel

The Phillips Curve: A Dilemma for Public Policy  
Inflation Versus Unemployment

Keeping Pace with the Nation: Third District  
Economic Trends in 1968

Monetary Policy: Lessons for the Future



# Monetary Policy: Lessons for The Future

by David P. Eastburn

This is a particularly appropriate time to recall the saying that those who do not learn from history are condemned to repeat it. In the field of monetary policy at least five important lessons can be learned from 1968. None of them is new. All of them, unfortunately, involve problems that hold little hope for complete solution except over a considerable period of time. But they are so basic that monetary policy cannot be entirely effective until they are solved.

## **Lesson #1. Monetary policy cannot count on timely and flexible fiscal policy.**

A good part of the problems encountered by the Federal Reserve in 1968 can be attributed to failures of fiscal policy. During the latter part of 1967 and the first half of 1968, the Federal Reserve, anticipating and hoping that Congress would increase taxes, did not move so vigorously to slow down expansion of money and credit as it might have.

Although belatedly, Congress did act. This fact, plus the tax cut of 1964, indicates that progress can be made in the future toward more flexible use of fiscal policy. But it also suggests strongly that progress will be disappointingly slow.

In formulating policy, the Federal Reserve authorities will not be able to count on timely and flexible fiscal action. As a result, money at times may be tighter than would otherwise be the case.

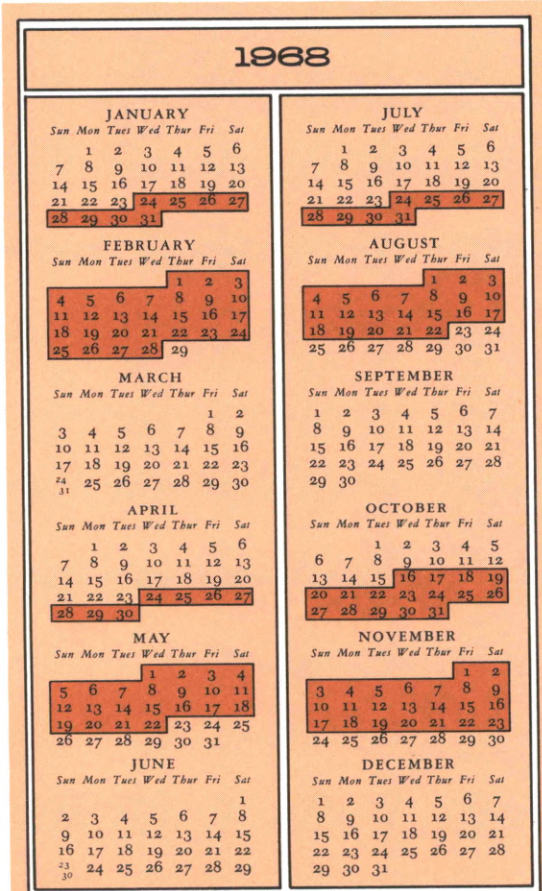
## **Lesson #2. Lags require good forecasting.**

Monetary policy is more sophisticated than it has ever been. There was a time when policymakers would have been delighted with the quantity and quality of economic information they are now getting on the recent past. Now, because the Federal Reserve increasingly recognizes that monetary policy acts with a lag, it is concentrating more and more on information about the future. There is little agreement on what the lag is, but there is a consensus that policy no longer can be formulated simply on the basis of the recent past.

*(Continued on Page 23)*

# Monetary Policy, Debt Management, and Even Keel

by Warren J. Gustus



EVEN-KEEL PERIODS

## EVEN KEEL, 1968

In 1968, a year of strong inflationary pressures, the Federal Reserve maintained a policy of even keel during six Treasury financings—i.e., a policy of no major change in monetary policy. As the calendar indicates, eight of the 12 months had even-keel periods in them.

The article following focuses on the policy of even keel against the broader backdrop of the relationship between monetary and debt management since the end of World War II. And it looks at some of the costs and benefits that even keel may entail.

The monetary historian has no difficulty in finding examples to demonstrate that control over the money supply has been a dangerous power to entrust to government. On the other hand, he also can give abundant reasons why control cannot be placed in private hands. For centuries, people throughout the world, including in the United States, have feared that government would resort to the printing press to finance its expenditures. And as recurring inflations have shown, the fear has not been unfounded.

In this country, until 1914, central banking and Treasury operations were not separated. The Treasury had long exercised central banking powers which were no less potent because they were not so labeled. But in 1914 a somewhat novel attempt to solve the problem of monetary control was begun with the formation of the Federal Reserve System as an agency

with quasi-independent status within the Government. Nevertheless, it is clear that the people who wrote the Federal Reserve Act did not believe the central bank can be independent of the Government. Nor have subsequent officials of the Federal Reserve and the Treasury believed it. From inception of the Federal Reserve, both it and the Treasury have been constantly adapting to each other and developing working relations in areas of joint responsibility. One such area is debt management.

Still, for many years, problems of coordinating debt management and monetary policy were minor ones. Thus, when the Federal Reserve was founded the public debt was small and problems in its management were slight. The fiscal ideal was a balanced budget. In large measure, monetary management was to be achieved automatically through operation of the international gold standard.

Now with a federal debt in excess of \$300 billion and a federal budget amounting to 20 per cent of national income, it is clear that coordination of monetary and debt management policies is essential. It is not always so clear how they should be coordinated nor what the priorities should be in the event they conflict with each other.

### **Post-World War II developments**

During World War II and for a number of years afterward, the Federal Reserve supported prices of Government securities and assured the success of Treasury financings at those prices. At first the overruling priority was to see that lack of funds did not impede effective prosecution of the war. Later, the concern was that abandonment of support would create great disruption in the market for Government securities and seriously upset the economy. By 1951, however, it had become clear that pegging the

price of Government securities meant loss of monetary control. Banks could obtain additional reserves merely by selling securities to the Federal Reserve at the pegged price. Consequently, the Federal Reserve and the Treasury negotiated an Accord which provided for discontinuance of all-out support of prices of Government securities.

Even after the Accord the Federal Reserve continued for a while its support policy when the Treasury was raising new money or refunding an outstanding issue. But in December, 1952, support of Treasury financings was discontinued as well.

The Federal Reserve then re-examined the whole question of its operations in Government securities markets, and in 1953 established operating policies limiting its intervention in them. One of these policies was that:

Operations for the System Account in the Open Market, other than repurchase agreements, shall be confined to short-term securities purchases (except in the correction of disorderly markets), and during periods of Treasury financing there shall be no purchase of (1) maturing issues for which an exchange is being offered, (2) when-issued securities, or (3) outstanding issues of comparable maturities to those being offered for exchange.<sup>1</sup>

A major purpose of this policy was to promote a free, self-sustaining market for Government securities and to avoid the possibility of again pegging the market. This policy was strictly adhered to except for two occasions, in 1955 and 1958, when the market had become disorderly.

In 1961 the Open Market Committee discontinued the statement of operating policies adopted in 1953. The reasons for this were

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<sup>1</sup> See policy record of the Federal Open Market Committee, September 24, 1953.

several, including the belief that an original purpose for publishing the policies had been achieved, i.e., to help in defining more clearly the System's operations in the Government securities market and in facilitating the transition from a rigidly controlled to a freer market. But in discontinuing the statement, the Open Market Committee made clear that this was not a decision to change the basic position of the System in relation to the Treasury or the market. It had no intention of pegging Government securities prices or of creating artificial conditions in the market when the Treasury was conducting financing operations.

### The policy of even keel

In short, from the end of World War II down to 1961, the Federal Reserve was engaged in a series of steps to re-order priorities. In the process, it shook off the commitment to peg prices of Government securities—a policy which had hobbled its ability to regulate money and credit. But the Federal Reserve, like other central banks, has continued to feel a responsibility not to complicate the Treasury's job of managing the debt. This responsibility is expressed in the term "even keel." To quote from an official publication:

While the System has believed that its power to create money should not be used to support these financings, it has recognized that concurrent monetary actions may affect their success. Consequently, the Federal Reserve has come to pursue whenever feasible what is known as an 'even keel' monetary policy immediately before, during, and immediately after Treasury financing operations.<sup>2</sup>

Although even keel dates back a number of

years, its significance has increased recently. One reason is that with the growth of inflationary pressures many have been concerned with the constraint it may pose for monetary policy. In addition, the Treasury has had to come to the market to raise large amounts of new money to finance substantial budget deficits. A further complicating factor is the decline in average maturity of the federal debt, and the implications this may have for the frequency of refunding operations. Average maturity has been decreasing because the Treasury has not been able to sell long-term debt at interest rates above the 4¼ per cent ceiling imposed by law.<sup>3</sup>

In light of these considerations, questions have been raised about the need for even keel, its costs, and its benefits.

### What is even keel?

Both in definition and practice, even keel is an elusive concept. In general, most market participants understand that even keel is a policy by the Federal Reserve of avoiding actions during Treasury financings that would signify a shift in monetary policy. Even keel is a commitment to neutrality by the Federal Reserve, but this commitment is particularly important to the Treasury during periods of monetary restraint. Then a move toward more restraint might involve higher interest rates and capital losses to Government securities dealers underwriting the issue. It could even trigger a failure of the financing.

Under most circumstances, even keel means no change in the discount rate and no change in

<sup>2</sup> *Federal Reserve System: Purposes and Functions* (Washington, D.C.: Board of Governors of the Federal Reserve System), November, 1966, pp. 38-39.

<sup>3</sup> Currently, the problems are not unique that the ceiling has created for debt management. Thus, during 1959-1960, the rate ceiling was restrictive. At the same time, the maturity schedule was heavy and a record budget deficit occurred in fiscal 1959. Further, the Treasury was having to finance a seasonal deficit. But this does not make them any the less troublesome.

reserve requirements because these moves are visible evidence of a policy shift. It generally means that the Federal Open Market Committee will adopt neither a more nor a less restrictive policy, and that actual operations will be conducted in such a way as to suggest no policy change to the market.

Beyond these rather general concepts, even keel becomes more difficult to define. It depends to a great extent upon the market situation prevailing at the time. Although the aim is to keep reserve availability roughly the same, with free or net borrowed reserves and federal funds fluctuating in a fairly narrow range, a greater-than-normal (or less-than-normal) supply of reserves may be necessary to keep the money market steady. From an operational viewpoint, during periods of even keel open market operations are conducted so as to maintain a steady tone in the money market.

Even keel usually begins a few days before announcement of a Treasury financing and continues until a few days after payment and delivery of the securities. In the period before announcement of a financing and its terms, the Treasury is canvassing the possibilities. Any change in market conditions then would make it more difficult for the Treasury to tailor the issue to meet its own needs and those of the market. Between announcement and delivery, the market is deciding on its subscriptions. From the Treasury's viewpoint, this is the most critical period because the success of an issue is determined then. The period after the books close and while an issue is being distributed is important because of the implications for future Treasury financings. If dealers see the value of their holdings undermined as a result of a change in monetary policy, they may be reluctant to participate in future offerings, particularly if one comes along soon.

### **Reasons for even keel**

The Government securities market is a key market in the economy, with particular importance for the Federal Reserve and the Treasury. The Treasury raises new money there and refinances outstanding securities; private investors use the market to adjust their liquidity and as an investment outlet; and the Federal Reserve uses this market in conducting open market operations, one of the major instruments of monetary policy.

Most of the transactions are effected through dealers, one of whose functions is to make markets by buying and selling securities for their own accounts. These dealers must be willing and able to maintain inventories of securities to accommodate customers when there are no immediate offsetting transactions. They are a key element in a key market.

There are relatively few dealers, all of them operating with slender equity-to-total-funds ratios and handling very large flotations of securities. Without even keel, they might suffer windfall profits or losses as a result of changes in monetary policy during Treasury financings. For example, if an increase in monetary restraint and a sharp increase in interest rates were to occur before dealers had distributed an issue to investors, the markdown in their holdings could cause them serious financial difficulties as well as making them reluctant to underwrite succeeding issues. On the other hand, an easing of policy that brought about a decline in interest rates could result in windfall profits not justified by any economic function the dealers perform.

### **Impact of even keel**

Government securities dealers have come to expect and depend on even keel. The Treasury

relies on it in conducting its financings. The Federal Reserve recognizes even keel as part of its responsibility as a central bank. Thus, there are strong reasons for its existence and continuation. Nevertheless, it is also important to consider the implications of even keel for monetary policy.

Economists agree that lags exist between a change in monetary policy and the full effects of the change. They do not agree on the duration and variability of the lags. In view of this uncertainty, it is hard to make a strong case that postponement of a change in monetary policy for several weeks does much harm. However, when the Treasury is in the market frequently, postponement of policy changes may have more serious consequences.

In considering the impact of even keel on timing of monetary policy, one must allow also for the interval needed to accomplish a shift in policy. About three free weeks between even-keel periods is the minimum necessary for the Federal Reserve to act. A week or two usually is required for the market to become aware that policy has been changed. Of course, if the policy change involves a change in the discount rate or in required reserves, recognition is instantaneous. Most of the time, however, open market operations are the policy tool used and they involve a lag between change in policy and recognition of the change. An additional week may be desirable to allow the market to adjust to a new policy; otherwise the Treasury could face considerable difficulty in financing in a market not fully adjusted to a shift in Federal Reserve policy.<sup>4</sup>

Much of the time when even keel is in effect the Federal Reserve would not want to change

<sup>4</sup> Even if the policy shift is toward ease, the financing could be complicated because of uncertainties about the appropriate price and terms for an issue.

policy anyway. To count up the duration of even keel and the time necessary to bring about policy shifts, therefore, may overstate the constraint on monetary policy. But even when a change in policy is not the issue, even keel may result in rates of growth in money and bank credit that are undesirable in terms of economic stability. The reason is that during even-keel periods the primary monetary policy objective is to maintain stability in money market conditions. As a result, bank reserves, money and credit have to be allowed to grow at whatever rate is consistent with money market stability. Sometimes these rates of growth will be consistent with those necessary to accomplish monetary policy goals but sometimes they will not.

Of course, the Federal Reserve can attempt to make compensatory changes in monetary policy outside of even-keel periods. For example, if a slowdown in growth of money and credit has to be postponed for, say, three weeks, policy can concentrate the desired changes at the end of the even-keel period. Sometimes, this is the case; and when it is, even keel poses no great problem for the timing of monetary policy. But when the Federal Reserve wishes to pursue a gradually more restrictive policy, sustained or frequent periods of even keel make it more difficult to compensate later for inaction. A danger is that sudden and sharp policy shifts will cause disruptions in money and credit markets.

### Looking to the future

For more than a half-century since the Federal Reserve was formed, ways have been sought for better coordination of debt management and monetary policy. Nor is it likely that this evolutionary process has been completed. Given even keel as the latest manifestation of this broad problem, what might be the path of the future?

One way of coordinating debt management and monetary policy, of course, would be to consolidate responsibility for them in one agency.<sup>5</sup> On economic grounds, such an arrangement has much to recommend it, but in the foreseeable future, at least, any changes will be much less radical.

A constructive and feasible step—once Congress becomes convinced of the need—would be to eliminate the 4¼ per cent ceiling rate on Government securities with a maturity of more than seven years. In June, 1967, Congress redefined Treasury notes to include maturities out to seven years instead of just to five. Since the 4¼ per cent rate ceiling does not apply to Treasury notes, the new legislation permitted debt managers some more leeway. However, with a three months Treasury bill now yielding above 6 per cent, the leeway is gone. In recent years the Treasury has been unable to sell longer-term debt at the ceiling rate, issuing instead shorter-term securities to which the ceiling does not apply. As a result, the average maturity of the debt has been declining. At the end of October, 1968, the average maturity of marketable interest-bearing public debt was down to the 10-year low of four years. Almost 49 per cent of this debt was due within a year.

The ceiling has not accomplished its purpose of minimizing debt costs. For one thing, the Treasury was not able to take advantage of the lower rates a few years back, while at the same time lengthening the debt. Rates then, while lower, were still above the ceiling. In addition, non-interest costs of the debt may have been increased if more frequent refundings and

hence higher flotation costs result from the shortened maturity of the debt.<sup>6</sup>

Within the limitations of its powers, the Treasury is constantly trying to regularize financings and reduce uncertainties associated with them. With a typical financing running into the billions, anything that reduces uncertainty about the timing, amount, and type of financings is desirable. To the extent that uncertainty in these areas can be decreased prior to announcement of a financing, money market conditions should become more stable during financings and the need for even keel less. In fact, the Treasury in recent years has made considerable progress in achieving more systematic debt management, including the regular rollover of bills and the raising of new funds by increments to the bill auctions, neither of which has been regarded as requiring an even-keel policy.

A less promising possibility in the future is shortening the duration of even-keel periods.<sup>7</sup> From 1959 to 1968 a few even-keel periods have been as short as 19 work days and a few as long as 30 days or more. But the heavy concentration of even-keel periods between 22 and 24 days over this long a time span suggests that chances for shortening its duration may be limited.<sup>8</sup>

The Federal Reserve has established some precedent for flexibility in policy during an even-keel period. For example, the policy directive covering open market operations from

<sup>6</sup> Flotation costs are hard to compute because much of these are not out-of-pocket. Nevertheless, they are costs as real as the interest on the debt.

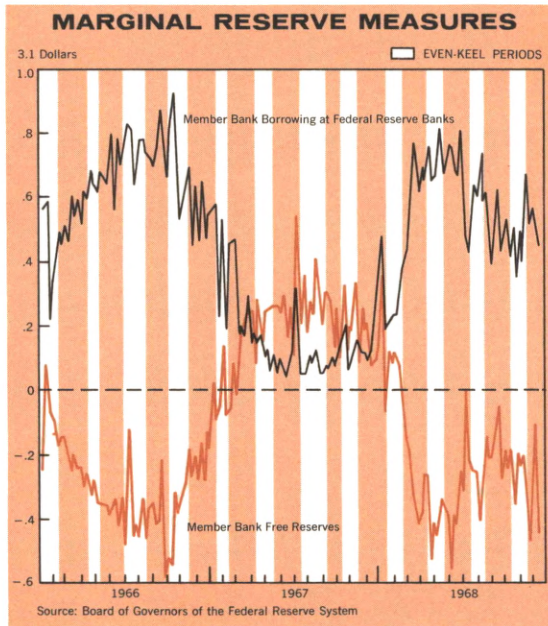
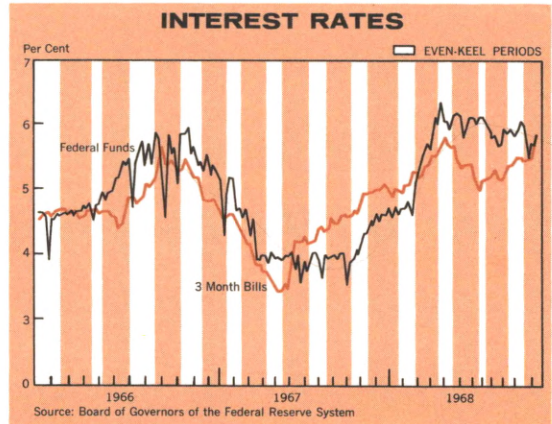
<sup>7</sup> Duration of even keel has been estimated by adding five work days before announcement of a financing and five work days after delivery of securities to number of work days between announcement and delivery. In practice, even-keel duration after delivery may vary from five days depending on such things as size of issue, dealer inventories, and market expectations.

<sup>8</sup> Over 50 per cent of the even-keel periods between 1959 and 1968 lasted 22 to 24 days. Only about 20 per cent lasted fewer days than this.

<sup>5</sup> Under one variant of this proposal the Treasury would borrow any funds it needed from the Federal Reserve and use any excess receipts to repay it. The Federal Reserve would be responsible for buying and selling securities in the market to attain monetary objectives.



February 7, 1968 to March 5, 1968 was to maintain firm conditions in the money market but to modify operations to the extent permitted by Treasury financing if bank credit appeared to be expanding as rapidly as pro-



jected. As the charts show, even keel has not, in fact, meant fixity of particular money market rates. While the main thrust of operations is reflected in relative stability of rates on federal funds and dealer loans, and in marginal reserve measures, these variables have fluctuated within even keel. Still wider fluctuations may be practicable.

Another possibility would be for the Federal Reserve, in rare and particularly difficult circumstances, to support a Treasury financing by direct purchases but offset this operation by open market sales. For example, in August,

1950, the Board of Governors and the Federal Open Market Committee announced their intention: “. . . to restrain further expansion of bank credit consistent with the policy of maintaining orderly conditions in the Government securities market.”<sup>9</sup> Later, the Open Market Committee purchased \$8 billion of Government securities maturing on September 15 and October 1 to assure the success of a Treasury refunding operation. At the same time, the System made sales of other securities from its portfolio to offset the additions to bank reserves.

All this took place before the Federal Reserve and the Treasury had reached their Accord in March, 1951. The kind of circumstances which gave rise to the action would not be present when the operations of both agencies are coordinated as well as now. Nevertheless, other situations might conceivably arise which would require a sudden change in monetary policy in the midst of a Treasury financing operation. If so, the earlier example illustrates how the Federal Reserve could prevent an offering from failing and yet accomplish its monetary objectives.

<sup>9</sup> See *Thirty-Seventh Annual Report of the Board of Governors of the Federal Reserve System*, p. 2.

**SUMMING UP**

The experience of the past quarter of a century, viewed against the backdrop of monetary history, demonstrates that the relation between treasuries and central banks continues to change. The relevant question is not now nor has it been whether the Federal Reserve should be independent of the Treasury or subservient to it. Thus, even so dramatic a development as

the Accord in 1951, looked at closely and in light of subsequent developments, turns out to be a re-ordering of goals rather than an assertion of independence by the Federal Reserve. The relevant question is how to order policy priorities and effect compromises at a minimum cost to the economy. The policy of even keel involves one of the areas of priority and compromise.

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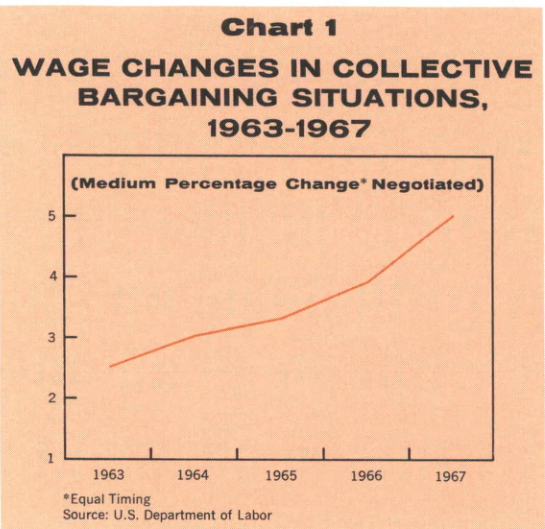
# The Phillips Curve: A Dilemma For Public Policy

## Inflation versus Unemployment

by Sheldon W. Stahl

It is probably common knowledge among many that the present economic expansion far exceeds any other sustained advance recorded in United States economic history. Yet, increasingly, amidst unparalleled prosperity and with a high likelihood of its continuance, a growing chorus of public and private discontent is being heard. For a concomitant of the high rates of economic growth in recent years has been price inflation—a phenomenon perhaps better known to most than the longevity of the expansion.

For those who make public policy, countering inflation will rank high in terms of priorities. At the private level, concern also is high. For example, at its meeting in October, 1968, the Business Council—an organization composed primarily of the heads of the largest business corporations in the United States—was reported to have endorsed the view that unemployment rates of 5 to 6 per cent should be tolerated in order to fight inflation. Although such proposals are not likely to serve as guidelines to public policy, they do dramatize what may well be the major economic problem facing policymakers in 1969—the trade-off between unemployment and inflation.



### WAGES, PRICES, UNEMPLOYMENT, AND PROFESSOR PHILLIPS

The American economy has been expanding for nearly eight years, but the past three have been marred by a departure from relative price stability. As Chart 1 shows, since 1965 the economy has experienced an accelerated upward pressure on wage rates. During the first nine months of 1968 the average annual rate of increase in wages and benefits in major collec-

tive-bargaining settlements was about 6 per cent. First-year wage adjustments were approximately 7.5 per cent as compared to less than 6 per cent for 1967. Thus, wage pressures not only continued in 1968, but actually intensified.

Throughout much of the postwar period, in fact, the behavior of wages has closely paralleled that of prices. During periods of inflation, wages tended to rise more rapidly than at times of relative price stability. This pattern has suggested to many observers a causal relationship between wages and prices, with wage increases putting pressure on costs and subsequently exerting an upward push on prices. A second hypothesis held that even in those instances where wages might not initiate price inflation, they necessarily had to follow price rises. Otherwise, aggregate demand could not be sustained at the new higher level; without the wage validation of price increases, the inflationary process would be terminated.

Current theories of inflation are an amalgam not only of these two hypotheses but of other non-wage explanations as well. Nonetheless, growing recognition of the vital role of wages in price determination as well as recent wage-price developments have imbued the whole process of wage determination with a heightened element of public interest.

The pivotal role of wages in the inflation equation has led to increasing familiarity with the term "Phillips curve." Working with data for Great Britain, Professor A. W. Phillips examined the relationship between aggregate unemployment and aggregate money wage rates.<sup>1</sup> He found a clear link between the two variables, with higher rates of wage gains associated with

lower rates of unemployment. The regression curve which described this relationship has come to be known as the Phillips curve, although this same term is often used to depict the relationship between rates of unemployment and price changes rather than wage changes.

Simply stated, Phillips and others found that low rates of unemployment tend to be associated with large wage increases of an inflationary character. Thus Government policymakers during such periods are confronted with the dilemma of choosing between some admixture of unemployment and inflation, and must try to adjust the level of aggregate demand to attain this mix.

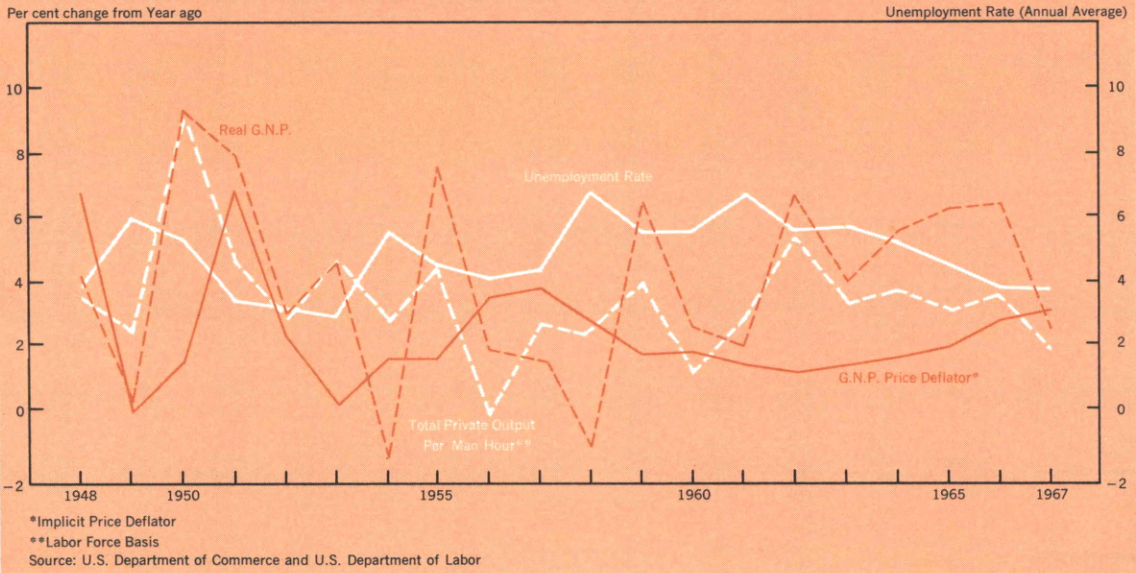
### **The productivity factor**

Chart 2 shows annual changes in real Gross National Product, prices, and productivity, compared to the unemployment rate during the period 1948-1967. The data suggest that lower rates of unemployment usually are generated by high rates of aggregate economic growth. Higher unemployment, on the other hand, usually is associated with low rates of growth. In 1950, 1955, 1959, and in 1962, when rapid growth failed to lower unemployment sharply, the explanation is found primarily in the behavior of output per manhour. In each of these instances, the economy was recovering from a period of recession, and initial gains in industrial productivity and in hours of work were very large. Gains in employment tended to be small relative to increases in output, since output could be increased with few added workers. At the same time, however, the rise in prices in these years, as measured by the G.N.P. price deflator, was about one-half as great as the average for 1948-1967, as both unit labor costs and prices benefited from the salutary effects of higher productivity.

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<sup>1</sup> A. W. Phillips, "The Relation Between Unemployment and the Rate of Change of Money Wage Rates in the United Kingdom, 1861-1957," *Economica*, November, 1958, pp. 283-299.

**Chart 2**  
**SELECTED ECONOMIC INDICATIONS, 1948-1967**



Although increased productivity does dampen somewhat the short-run gains in employment as the economy grows, it is vitally important both to relative price stability in the long run and ultimately the longevity of the economic advance itself. In fact, much capital investment is motivated by the desire to enhance longer-run productivity. To be sure, even with modest gains in productivity, price stability can be maintained if wage demands are modest. However, the farther along the economic advance, the smaller are the gains realized in productivity as margins of idle plant capacity are absorbed and workers with requisite skills become increasingly scarce.

These are precisely the circumstances which give rise to the relationship between wages and unemployment observed by Phillips. When aggregate demand is growing and productivity

gains are moderating, the relative demand for labor intensifies as the supply of labor becomes tight. Lower unemployment is reflected in aggressive wage demands and large wage gains push unit labor costs—and prices—upward. Each successive increase in consumer prices becomes part of the rationale for new and higher wage demands.

### The recent record

This process largely explains what has happened to the American economy since mid-1965. Following the 1960-61 recession, the economy made considerable inroads into the pool of unemployed labor. In 1965, unemployment had dipped below 5 per cent of the labor force, and the margin of unutilized manufacturing plant capacity had declined to the point where there was little slack to accommodate new demand.

It was at this point that the Vietnam war escalated. The pressure of this sizable additional demand, compressed into a relatively short time, had predictable consequences. Wage and price increases accelerated sharply. Unemployment fell significantly through early 1966, then became locked into a narrow range of movement. As Chart 2 shows, unemployment averaged 3.8 per cent of the labor force both in 1966 and 1967. For the year 1968, the over-all unemployment rate was somewhat lower.

Events of the past three years have shown that when the unemployment rate falls below 4 per cent, additional injections of spending beyond the real productive capabilities of the economy carry—for most of us—an unacceptably high cost in terms of inflation.

### Another view

However, there are those who might regard the costs of inflation as acceptable if unemployment could further be reduced. Since further reductions would primarily benefit the disadvantaged, such a view should not be dismissed lightly. It is true, of course—as the experience of World War II and the Korean War clearly show—that unemployment could be forced below present levels, given sufficient stimulation of the economy.

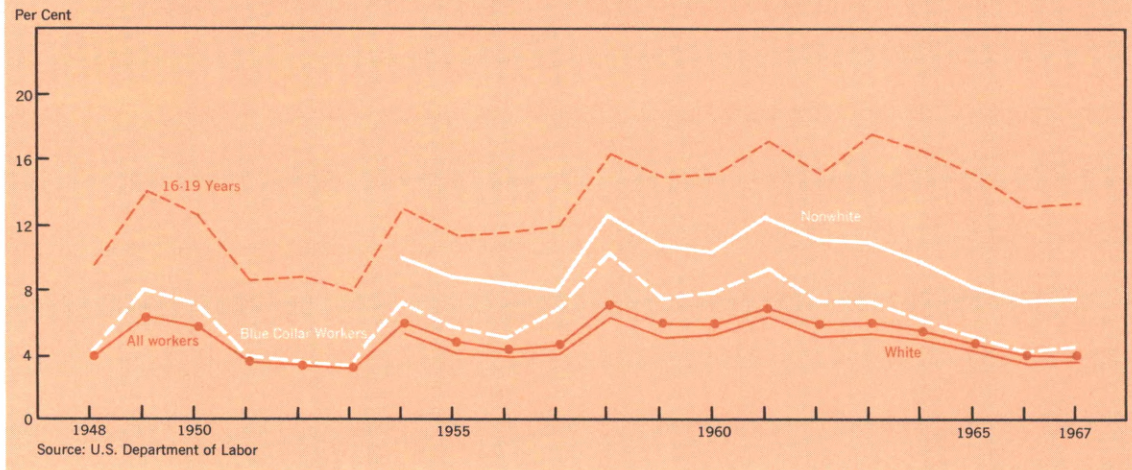
However, the accomplishments of a wartime economy under a comprehensive set of controls allocating materials and labor, and limiting wage and price increases, are not appropriate standards. Without Government controls, explicit price increases during these wars would have been much greater than they were. Recent experience suggests that price increases in the 3 to 4 per cent range have not been associated with a substantial lowering of unemployment from levels of three years ago.

Moreover, there is the real question of what rate of inflation would result if public policy aimed, for example, merely at *holding* unemployment within a range of, say, 3½ per cent to 4 per cent. Past relationships as expressed in a given Phillips curve may indicate that at times this range of unemployment has been accompanied by annual price increases of more than 4 per cent. But, how long would prices rise by 4 per cent if it became generally known that this was public policy? For example, would labor unions, anticipating sustained inflation, increase their wage demands by amounts at least equal to expected price rises? Would producers' demands for new plant and equipment become increasingly a function of expected increases in the prices of these goods? Would wholesalers and retailers attempt to beat expected price hikes by laying in inventories in excess of those warranted by current sales levels? In short, would the expectation of continued inflation lead to greater inflation?

There would seem to be ample evidence that when expectations of continued inflation become widespread, events such as those hypothesized above do, in fact, occur. Thus, inflation spirals and becomes self-reinforcing. The Phillips curve is a static concept; while inflation is a dynamic process. Once inflation is accepted as public policy, the Phillips curve on which such a policy may be predicated would shift adversely in response to spiraling price increases.<sup>2</sup> This illustrates the danger in trying to base public policy on an assumed static relationship between unemployment and price changes when, in fact, the relationship may continually be shifting.

<sup>2</sup> An adverse shift in the Phillips curve means that any given rate of unemployment would be associated with a higher rate of price increase; or, for any given rate of price increase, there would be associated a higher rate of unemployment.

**Chart 3**  
**SELECTED UNEMPLOYMENT RATES, 1948-1967**



### What might be done?

If continuing inflation is not to be tolerated, what can public policy do? And what are the implications of these choices? One method of dealing with this problem is to impose Government controls on prices and wages. This choice, however, is highly undesirable. Such controls, especially in the absence of extreme wartime conditions, are both anathema and of questionable effectiveness. Non-price rationing, in place of the market mechanism, distorts the whole pattern of rational allocation of resources. Experience has shown that the imposition of general price-wage controls inevitably leads to evasion and spawns a proliferation of increasingly specific controls. The costs to our economic system might well exceed whatever benefits such controls might bestow.

An alternative to wage-price controls is the strategy of trade-off—trying, through monetary and fiscal policy actions, to slow down the rate of growth in the economy in order deliberately to create slack and remove some of the pressure on resources, particularly labor. This means

acceptance of temporarily higher levels of unemployment in order to slow down inflation.

### BEHIND THE PHILLIPS CURVE

Although the concept of the Phillips curve may be helpful in trying to quantify the terms of the trade-off, it deals with a problem that has confronted public policymakers many times in the past. The really new element in the dilemma is the increased concern about the implications of the trade-off for different groups in our society. As over-all unemployment has declined during the economic growth of the 1960's, emphasis has shifted from overriding considerations of *how many* people are unemployed to the question of *who* are unemployed. Concern today is over where the heaviest burden of any trade-off, in terms of higher unemployment, will be borne.

Chart 3 clearly shows, for example, the striking disparity between the decline in joblessness for all workers and the experience of teenage workers. The persistent gap between whites and nonwhites is also apparent, with the latter

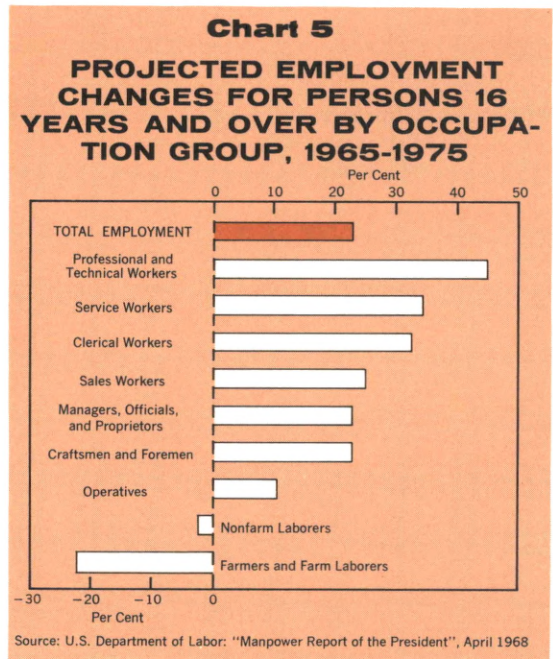
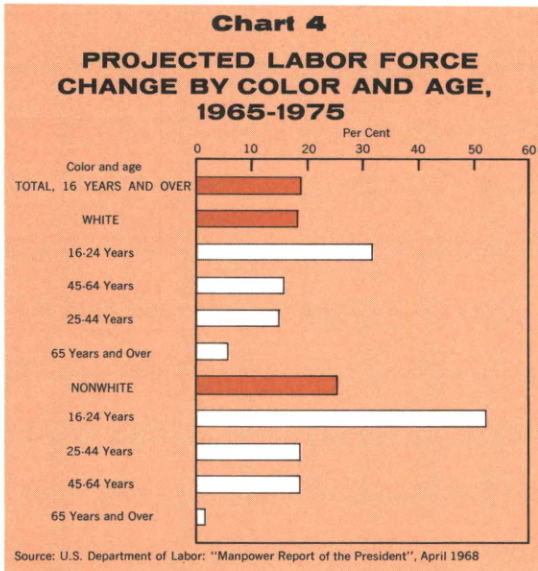
experiencing at least double the rate of unemployment of the former. And it shows that the fortunes of blue-collar workers, especially the semi-skilled and unskilled, are more adversely affected by economic recession than those of other groups. It is this disparate nature of unemployment that has to be considered in weighing the implications of any trade-off strategy. For sustained prosperity, while bringing about absolute improvements, has not greatly improved the relative positions either of the young (non-white youths in particular) or nonwhites generally. The burden of any rise in over-all unemployment will fall heaviest on these same groups. Since the disadvantaged include the least skilled and least productive, they are among the last to be hired when demand is strong and the first to be laid off when demand weakens. Furthermore, the experience of 1957-1958, when both economic recession and inflation coexisted, should temper the confidence of advocates of a sizable trade-off in fewer jobs as

a vehicle for bringing about a prompt arrest of inflation.

**Looking ahead**

Moreover, the problem is likely to become more severe in the future. As Chart 4 shows, nonwhites in the labor force are expected to increase much faster than whites. Young people—16 to 24 years of age—both white and nonwhite are expected to enter the labor force in especially large numbers. By 1975, nonwhites aged 16 to 24 years will account for more than one-fourth of the total nonwhite labor force, as compared to about one-fifth of the total a decade earlier. These are the least skilled and the least experienced in the labor force. Nonwhites in the most productive 25- to 44-year age group, on the other hand, will represent a smaller proportion of the labor force in 1975 than they did in 1965. This same pattern of change is applicable to the white component of the labor force as well.

Given this outlook on the labor-supply side,



**FUTURE LABOR SUPPLY IS OUT OF PHASE WITH FUTURE LABOR DEMANDS**



what are the employment opportunities which will confront this labor force? Unfortunately, the future employment profile, shown in Chart 5, is seriously out of phase with the labor-force profile shown in Chart 4. For example, opportunities are expected to be greatest for highly skilled professionals and technicians, and least for either semi-skilled or unskilled blue-collar workers. Although employment of skilled blue-collar workers is projected to rise by about one-fourth, participation of younger workers, and nonwhites in particular, in this growth appears quite limited because of lack of training or other barriers. Growth in both the clerical and service sectors may hold some promise for disadvantaged groups, although skill requirements would still present a formidable obstacle.

Thus, both for the near term and the somewhat longer term, the structure of unemployment will remind public policymakers that the attempt to purchase less inflation via rising unemployment has serious costs, both economic and social.

### **The fundamental solution**

Despite these costs, however, moderating inflation probably will entail rising unemployment, since such a trade-off seems unavoidable. The road back to price stability may not be short and a good deal of patience will be required. Recognizing this, public policy may be able to make the required trade-off more palatable. For example, if the time horizon for a return to price stability is lengthened, the costs in terms of higher unemployment rates might be minimized.

However long the adjustment process, a fundamental attack on those factors which have shaped the structure of unemployment is a must for a long-term solution. Intensification

of manpower training to upgrade the skills of the labor force and increase its productivity and earnings is one of the most-needed steps. Beyond this, elimination of barriers to labor mobility and discriminatory barriers to free entry into the job market, strengthening of competition, and recognition of the increasingly adverse impact of rising statutory minimum wages on employment of those with little skill would all be part of a simultaneous attack not only on unemployment but also on inflation itself. By increasing the productive resource base in these ways, such efforts not only would enlarge the real output potential of the economy, and thereby favorably shift the Phillips curve, but they also would bring more of the disadvantaged into the economic mainstream.

This joint approach represents, in part, an alternative either to direct controls or to a costly trade-off in terms of high unemployment. But the immediate problem remains that of a trade-off. The reality of inflation at present and the likelihood of its persistence in the months ahead, as well as the time needed to correct more fundamental structural problems, point toward some measure of rising joblessness as a likely cost of moderating inflation.

Perhaps the degree of price inflation or the pace of wage increases since 1965 would have been appreciably lower if aggregate demand had grown in a more orderly fashion. The economy might very well have been subjected to far less stress than it actually was. The lesson which clearly emerges from the experience of the past three years is that effective stabilization policy is not possible without a coordinated and responsive mix of both fiscal and monetary actions. With such a mix, applied at the right time—the need to choose between the Scylla and Charybdis of inflation or unemployment would be significantly reduced.

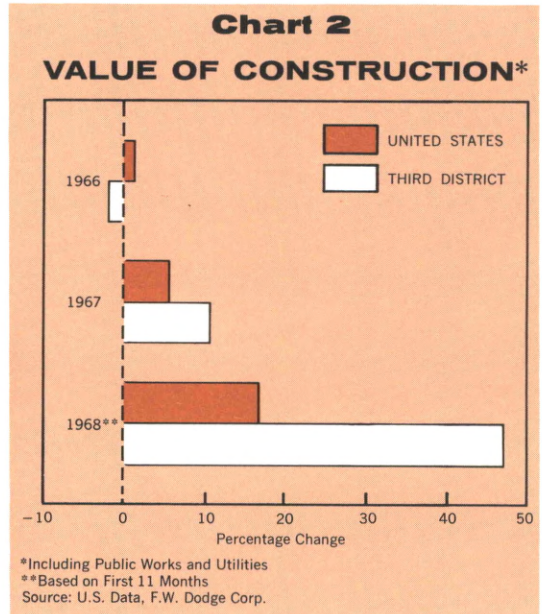
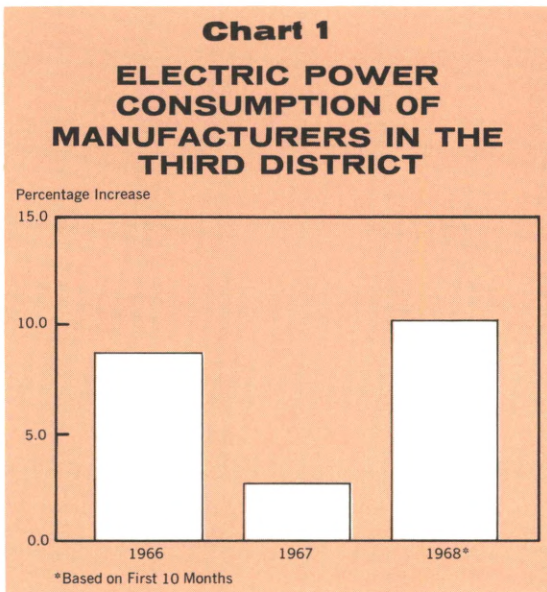
Economic activity in the Third Federal Reserve District during 1968 kept pace with the rapid advance of the national economy. Production and sales were strong and labor markets remained tight. Prices rose at a faster clip than for the nation as a whole. Loans, investments and deposits at member banks also advanced, reflecting national financial trends.

# Keeping Pace With The Nation: Third District Economic Trends in 1968

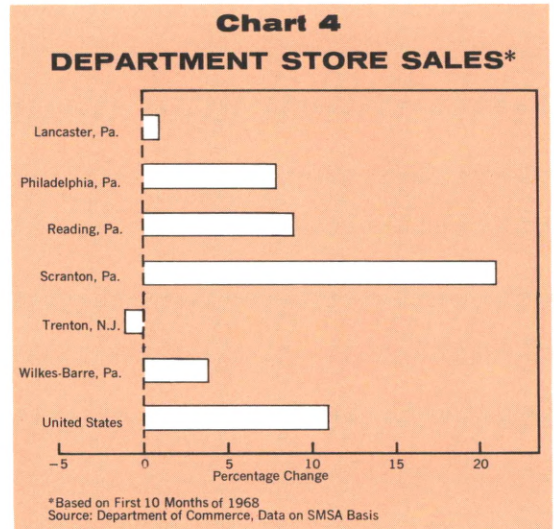
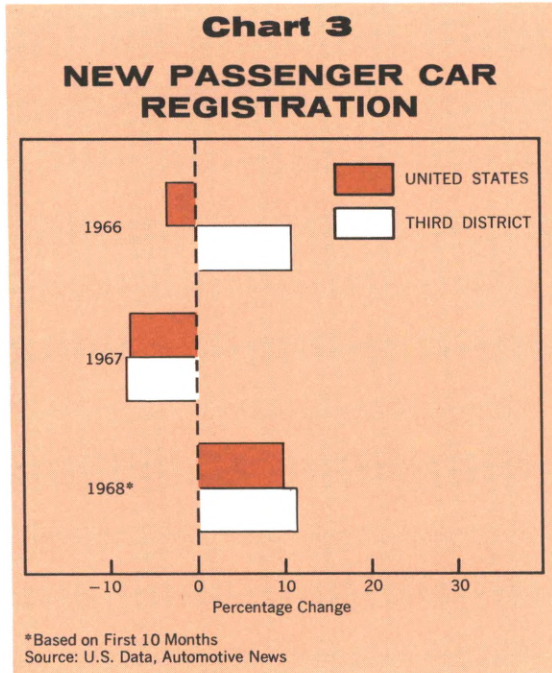
by Edward G. Boehne

### Production and sales

Workers in the Third District produced more goods in 1968 than during the previous year. As measured by electric power consumed by industrial firms, manufacturing activity in the district registered a substantial increase in 1968, rising 10.1 per cent over 1967 as shown in Chart 1.



Construction activity, including residential, nonresidential and public works, also showed considerable strength in the district, outpacing the nation as a whole. As indicated in Chart 2, construction nationally rose just over 17 per cent in 1968, while the district recorded an increase of just under 47 per cent. The 1968 rate of gain



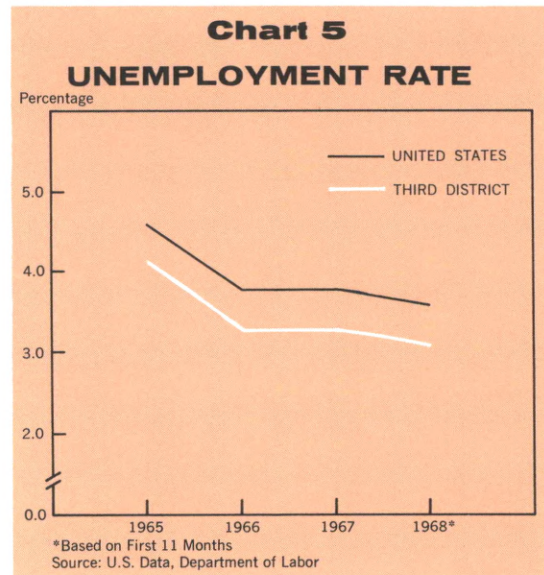
### Labor markets

Because of the vigor in business activity, labor markets in the Third District remained tight in 1968—even tighter than for the nation as a whole. As shown in Chart 5, the unemployment rate for the region was 3.1 per cent, down slightly from 3.3 per cent in 1967, and still one-half of 1 percentage point below the national average.

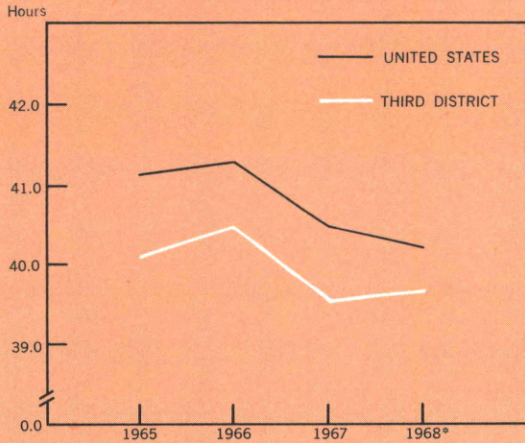
for the district boosted by a whopping 145 per cent rise in public works construction, was nearly quadruple that posted in 1967.

While people in the Third Federal Reserve District were producing more in 1968, they also were consuming more. For example, following a decrease in 1967, registration of new passenger cars (a rough proxy for new car sales) in the district rose by slightly more than 11 per cent in 1968—2 per cent higher than in the nation (Chart 3).

Also, department store sales in the Third District were strong in 1968; however, sales performance was mixed throughout the district as indicated in Chart 4. In Philadelphia and Reading, sales paralleled the nation while in Lancaster, Trenton and Wilkes-Barre they were considerably below, and in Scranton considerably above the national rate of growth.



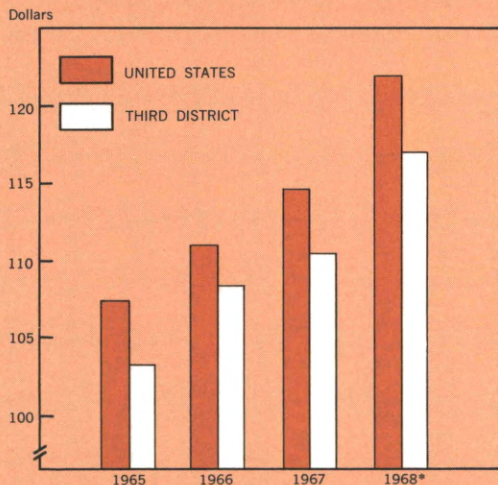
**Chart 6**  
**AVERAGE WEEKLY HOURS WORKED**



\*Based on First 11 Months  
Source: U.S. Data, Department of Labor

Employees in the district worked an average of 39.8 hours per week in 1968—about the same as they worked in 1967 (Chart 6). Nationally, the figure was slightly higher at 40.2, suggesting workers put in more overtime in the nation than in the district.

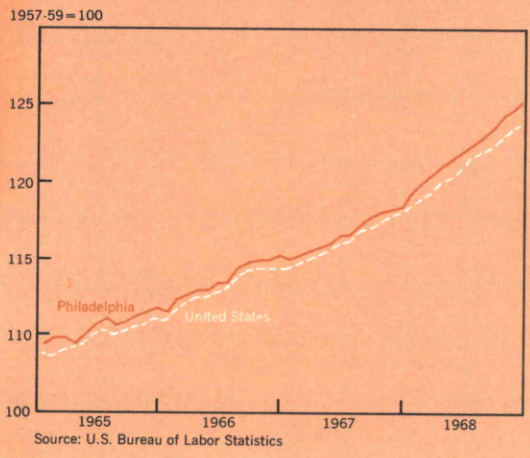
**Chart 7**  
**AVERAGE WEEKLY EARNINGS**



\*Based on First 11 Months  
Source: U.S. Data, Department of Labor

For those participating in the work force last year, earnings also set a new record as indicated in Chart 7. In the district, weekly earnings climbed an average of nearly \$6 per week in 1968 to \$117. The increase in the nation was \$7 and average earnings for the year were \$122 per week—\$5 higher than in the district.

**Chart 8**  
**CONSUMER PRICE INDEX**

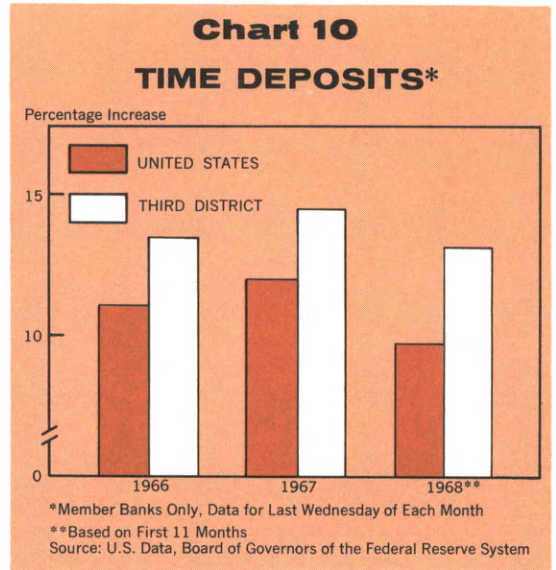
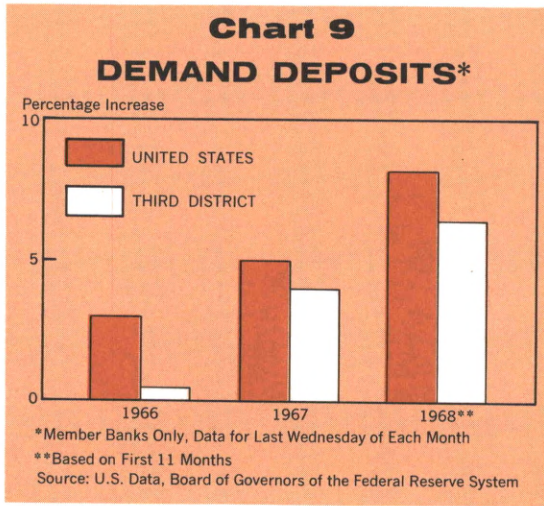


Source: U.S. Bureau of Labor Statistics

**Prices**

But along with a tight labor market and record wage levels also came higher prices. The Philadelphia Metropolitan Area experienced substantial inflation in 1968—even more than the nation as a whole. Consumer prices (Chart 8) jumped 6.3 per cent\* in the Philadelphia area compared to a national increase of 5.6 per cent.\* Consumer services continued to be in the vanguard of inflationary pressures.

\* November 1967 to November 1968.

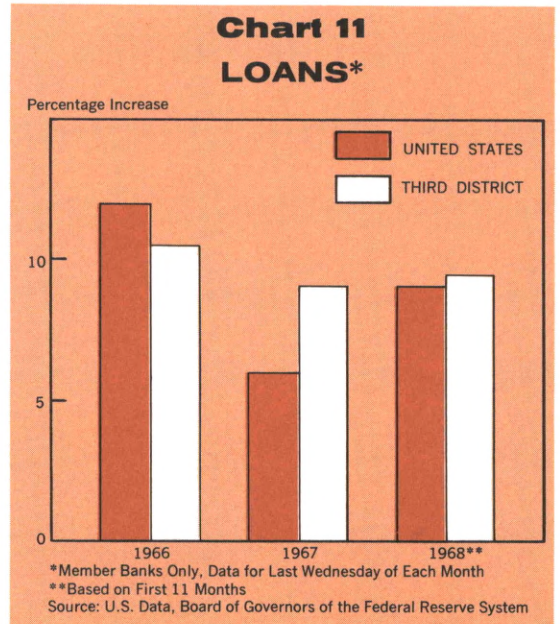


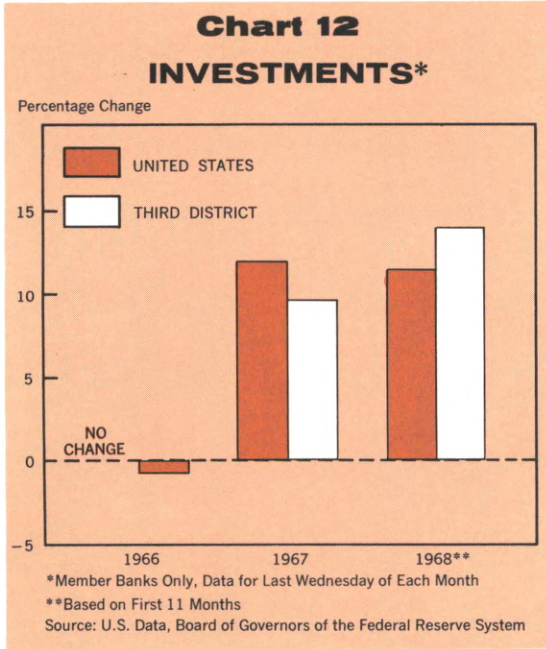
## Banking and finance

Banking trends reflected both robust business activity and conditions in the financial markets. As a result, banks experienced sharp increases in loans, investments and deposits.

At member banks in the Third Federal Reserve District, demand deposits and time deposits showed substantial advances in 1968 as shown in Charts 9 and 10. Compared to 1967, demand deposits were up 6.4 per cent in 1968 and time deposits 13.1 per cent.

Loan volume at Third District member banks jumped 9.8 per cent compared to a national increase of 8.9 per cent. Much of the advance was accounted for by the behavior of business loans.





Bank investments—holdings of U.S. Government and other securities (primarily state and local)—also moved up rapidly in 1968 (Chart 12). Nationally, bank investments chalked up an 11.1 per cent gain, while at Third District member banks investments increased 13.4 per cent from 1967 to 1968.

\* \* \*

In short, for the Third District as well as for the nation 1968 was a year of prosperity—record production, record sales, record wages, and record employment. But it was also a year of inflation—the most in nearly a decade and a half. How to regain some semblance of price stability without losing prosperity remains in 1969, as it was in 1968, the primary economic problem facing the nation and the district.

(Continued from page 2)

Unfortunately, as 1968 illustrates, ability to perform is not equal to desire. Very few economists, both inside and outside of the Federal Reserve, correctly foresaw the strength of the economy following the tax increase and spending cuts enacted by Congress at midyear. As a result, many who earlier were concerned about overkill are now worried about another burst of inflation in 1969. Had economists seen the outlook six months ago as they see it now, monetary policy quite possibly would have been more restrictive.

Here again, however, the solution will be slow in coming. Not only will economists have to learn much more about lags, but they will have to improve their ability to forecast the future.

### **Lesson #3. Multiple guides and objectives require trade-offs.**

Adherents to the quantity theory of money have found it hard to understand why the Fed permitted money to expand so rapidly at times in 1968. One explanation is the fact that increases frequently were greater than the Federal Reserve expected.

One reason for this, in turn, is that the money stock is not the only thing the Federal Reserve was trying to influence. The Board's staff does, as a matter of standard procedure, estimate by how much money and credit aggregates are likely to change in the short run, given certain conditions in the money market. These projections can miss, even if those money market conditions are maintained, whenever there is a shift in the relation between such conditions and the demand for money and credit.

This less-than-perfect ability to forecast the important variables is one price of multiple guides to policy. Life in the Fed would be much

simpler if single-minded attention could be given to one guide—whether the money stock or interest rates—and letting the market determine the value of all other variables. Because the Fed has an eclectic theory of linkages between policy action and economic behavior, it does not do this.<sup>1</sup>

A solution to the problem of conflicting guides to policy can come only over a period of some time. The day may arrive when economists can describe with reasonable certainty the relationships among the many variables involved. On that day, it won't matter whether policy guides are stated in terms of money stock, bank credit, interest rates, or whatever; one will serve as well as another.<sup>2</sup> Economists are a long way from the necessary understanding of the economy and financial system to make that possible.

The chances of solving the problem of trading off one *ultimate* objective against another are even more remote. Some policymakers will put more stress on full employment than stable prices. Some will give greater weight to international matters than others. Hopefully, economists will be better able to tell policymakers the consequences of trade-offs, but policymakers will still have to make the difficult value judgments.

### **Lesson #4. Even keel can be inflationary.**

During 1968, as the calendar in the first article in this Review indicates, the United States Treasury came to the market a number of times. Inasmuch as it is customary for the Federal Reserve to maintain an even keel in money mar-

<sup>1</sup> Most officials of the Federal Reserve have such a theory. In addition, since some individuals may emphasize one guide and some another, the combined result is an eclectic view.

<sup>2</sup> Of course, some may be more appropriate than others for operational reasons.

kets during Treasury financing operations, the Fed found itself constrained from making any major change in policy during a fair proportion of the year.

As the article points out also, an even-keel policy may mean that changes in policy are delayed, not taken at all, or more drastic and packed into a shorter period when they are taken. In 1968, the even-keel policy probably caused money to be easier than otherwise would have been the case.

This poses a logical question for the future. Given the likely increase in the public debt over the years to come and given problems of lengthening the maturity of the debt, an even-keel policy could at times hamper attempts to bring inflationary pressures under control.<sup>3</sup> Of course, the central bank cannot ignore the financial needs of its Government, but at the same time it must make sure it carries out its responsibility for monetary control. One lesson from 1968 is that ways might well be considered to lessen the inflationary implications of even keel in the future.

#### **Lesson #5. Competition solves many problems.**

Although not in the center of the stage as in 1966, disintermediation lurked in the wings for most of 1968. Concern about the effect of monetary policy on savings flows caused the Federal Reserve to be less restrictive than might have been the case otherwise.

It is easy to conclude that the simple lesson is to remove ceilings on interest rates on time and savings deposits. But the resulting impacts on savings institutions and the mortgage mar-

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<sup>3</sup> Although even keel works both ways—that is, it constrains monetary policy from easing as well as tightening—in practice it is not likely to be completely symmetrical. The greater problem is encountered on the restrictive side.

ket could be most severe. Monetary restriction does have unequal impacts on various parts of the economy, and the Federal Reserve can't overlook the fact.

The ideal solution to these unequal impacts is to work toward freer flows of funds among financial markets. Some minor progress in this direction since the 1966 crunch is indicated, for example, by the fact that usury laws have been changed and statutory interest-rate ceilings on FHA and VA mortgages have been removed, at least for the time being. However, when it comes to broadening the powers of savings and loans and mutual savings banks, equalizing tax burdens, and other such basic steps to heighten competition among the various types of financial institutions, there is solid resistance. The economists' idealized conception of a free competitive market for savings and mortgages is a long way off.

#### **THE OUTLOOK**

In examining the past to find lessons for the future, there is always a tendency for any institution to look for reasons beyond its control why things may have turned out less than perfectly. Yet it is a fact of life that in many respects the difficulties of 1968 stemmed from deep-seated problems which will take a long time to solve. We do not have a sufficiently flexible fiscal policy; we do have a great deal to learn about lags and about predicting the future; we do have multiple guides and objectives that often call for trade-offs; we do have a large and growing federal debt that must be financed; and we do operate in credit markets that are imperfectly competitive.

In 1969 these same problems will confront the Federal Reserve, some in even greater intensity.



- On the fiscal front the most important decision will be whether to extend the 10 per cent surcharge beyond June 30. Given the economic strength that now seems likely to prevail in 1969, the case for extension is strong indeed. Given recent experience with tax changes, however, it would be unrealistic for the Fed to make the easy assumption that extension will be accomplished.
  - Recognizing that despite the fiscal package, inflationary pressures were persisting, the Fed in late 1968 moved toward more monetary restraint. As the Federal Reserve determines policy early in 1969, it will be influencing the course of events later in the year and even in 1970. At that time, just possibly, the problem may be a weakening economy. The lot of the forecaster again will not be a happy one.
  - Moreover, the trade-offs among the various guides and objectives of monetary policy are likely to become even more difficult to make in 1969. What levels of interest rates might accompany efforts to slow growth of the money stock to, say, an annual rate of 4 per cent this year? No one can say now, but they might well be so high as to pose serious problems for financial markets. And as the second article in this Review indicates, policymakers will face even more starkly than in 1968 the trade-off between a stable dollar domestically and internationally and a low level of unemployment.
  - A silver lining in the clouds looming over 1969 is the likelihood that the Treasury will need to be in the market for funds less heavily, although perhaps not less frequently. Hopefully, there will be less constraint from an even-keel policy and more room for the Federal Reserve to maneuver.
  - Although demands from the Treasury may be less, a continuation of inflationary pressures would pose substantial problems for another sector—housing and mortgage markets. This was the area hardest hit by the credit crunch of 1966. If the Federal Reserve is obliged to tighten further in 1969, implications for housing could be especially great in view of the fact that housing needs have become more pressing relative to available supply than they were in 1966. Regulation Q seems destined to be in the spotlight again.
- Given the persistence of these complex and basic problems in 1969 and probably for some years to come, one group of observers has concluded that monetary policy would best be reduced to a simple rule: increase the money stock by some constant rate. A more realistic point of view is that these difficult problems call for even greater discretion, flexibility, and imagination than before.

## **DIRECTORS AND OFFICERS**

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At the election held in the fall of 1968, Mr. Harold F. Still, Jr., President, Central-Penn National Bank of Philadelphia, Philadelphia, Pennsylvania, was elected by member banks in Electoral Group 1 as a Class A Director for a three-year term beginning January 1, 1969. He succeeds Mr. Howard C. Petersen. Mr. Henry A. Thouron, President, Hercules Incorporated, Wilmington, Delaware, was re-elected by member banks in Electoral Group 2 as a Class B Director for a like term.

The Board of Governors of the Federal Reserve System redesignated Dr. Willis J. Winn, Dean, Wharton School of Finance and Commerce, University of Pennsylvania, Philadelphia, Pennsylvania, Chairman of the Board of Directors of this Bank and Federal Reserve Agent for the year 1969. Mr. Bayard L. England, Chairman of the Board, Atlantic City Electric Company, Atlantic City, New Jersey, was redesignated Deputy Chairman of the Board for 1969. Mr. D. Robert Yarnall, Jr., President, Yarway Corporation, Blue Bell, Pennsylvania, was reappointed a Class C Director for a term of three years beginning January 1, 1969.

The Board of Directors of this Bank selected Mr. George H. Brown, Jr., Chairman of the Board, Girard Trust Bank, Philadelphia, Pennsylvania, to serve during the year 1969 as the member of the Federal Advisory Council from the Third Federal Reserve District.

Appointments to officer positions in this Bank during the year included: Albert Spencer, Jr., Assistant Vice President on February 1; Hiliary H. Holloway, Assistant Counsel on June 19, Mark H. Willes and William F. Staats, Senior Economists, George C. Haag, Public Information Officer, and Eugene W. Lowe, Securities Officer, effective January 1, 1969. Also effective January 1, 1969, eight officers were promoted to new positions: Joseph R. Campbell, David P. Eastburn, David C. Melnicoff, and James V. Vergari, former Vice Presidents, to the newly created position of Senior Vice President; Warren J. Gustus, formerly Research Officer and Economist, to Economic Adviser; Sheldon W. Stahl, formerly Research Officer and Economist, to Senior Economist; D. Russell Connor, formerly Assistant Secretary and Building Officer, to Assistant Vice President and Assistant Secretary; and James A. Agnew, formerly Assistant Cashier, to Collections Officer.

**DIRECTORS AS OF JANUARY 1, 1969**

Group		Term expires December 31
	<b>CLASS A</b>	
1	HAROLD F. STILL, JR. President, Central-Penn National Bank of Philadelphia Philadelphia, Pennsylvania	1971
2	ROBERT C. ENDERS President, Bloomsburg Bank-Columbia Trust Co., Bloomsburg, Pennsylvania	1969
3	H. LYLE DUFFEY Executive Vice President, The First National Bank of McConnellsburg, McConnellsburg, Pennsylvania	1970
	<b>CLASS B</b>	
1	PHILIP H. GLATFELTER, III President, P. H. Glatfelter Co., Spring Grove, Pennsylvania	1970
2	HENRY A. THOURON President, Hercules Incorporated Wilmington, Delaware	1971
3	EDWARD J. DWYER President, ESB Incorporated, Philadelphia, Pennsylvania	1969
	<b>CLASS C</b>	
	WILLIS J. WINN, Chairman Dean, Wharton School of Finance and Commerce University of Pennsylvania Philadelphia, Pennsylvania	1970
	BAYARD L. ENGLAND, Deputy Chairman Chairman of the Board Atlantic City Electric Co., Atlantic City, New Jersey	1969
	D. ROBERT YARNALL, JR. President, Yarway Corporation, Blue Bell, Pennsylvania	1971

## **OFFICERS AS OF JANUARY 1, 1969**

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**KARL R. BOPP, President**

**ROBERT N. HILKERT, FIRST VICE PRESIDENT**

**JOSEPH R. CAMPBELL, Senior Vice President**  
**DAVID P. EASTBURN, Senior Vice President**  
**DAVID C. MELNICOFF, Senior Vice President**  
**JAMES V. VERGARI, Senior Vice President and General Counsel**  
**EDWARD A. AFF, Vice President**  
**HUGH BARRIE, Vice President**  
**NORMAN G. DASH, Vice President**  
**WILLIAM A. JAMES, Vice President**  
**G. WILLIAM METZ, Vice President and General Auditor**  
**LAWRENCE C. MURDOCH, JR., Vice President and Secretary**  
**JACK P. BESSE, Assistant Vice President**  
**JOSEPH M. CASE, Assistant Vice President**  
**D. RUSSELL CONNOR, Assistant Vice President and Assistant Secretary**  
**RALPH E. HAAS, Assistant Vice President**  
**WARREN R. MOLL, Assistant Vice President**  
**HENRY J. NELSON, Assistant Vice President**  
**KENNETH M. SNADER, Assistant Vice President**  
**ALBERT SPENCER, JR., Assistant Vice President**  
**RUSSELL P. SUDDERS, Assistant Vice President**  
**JAMES P. GIACOBELLO, Chief Examining Officer**  
**THOMAS K. DESCH, Examining Officer**  
**WILLIAM L. ENSOR, Examining Officer**  
**JACK H. JAMES, Examining Officer**  
**LEONARD E. MARKFORD, Examining Officer**  
**WARREN J. GUSTUS, Economic Adviser**  
**WILLIAM F. STAATS, Senior Economist**  
**SHELDON W. STAHL, Senior Economist**  
**MARK H. WILLES, Senior Economist**  
**JAMES A. AGNEW, Collections Officer**  
**SAMUEL J. CULBERT, JR., Bank Services Officer**  
**GEORGE C. HAAG, Public Information Officer**  
**HILIARY H. HOLLOWAY, Assistant Counsel**  
**EUGENE W. LOWE, Securities Officer**  
**A. LAMONT MAGEE, Assistant General Auditor**  
**DAVID P. NOONAN, Assistant Personnel Officer**

## STATEMENT OF CONDITION

### Federal Reserve Bank of Philadelphia

(000's omitted in dollar figures)	End of year	
	1968	1967
<b>ASSETS</b>		
Gold certificate reserves:		
Gold certificate account .....	\$ 494,258	\$ 560,613
Redemption fund—Federal Reserve notes .....	—	101,189
Total gold certificate reserves .....	\$ 494,258	\$ 661,802
Federal Reserve notes of other Federal Reserve Banks	35,064	48,728
Other cash .....	4,901	8,610
Loans and securities:		
Discounts and advances .....	100	1,430
United States Government securities .....	2,810,204	2,525,715
Total loans and securities .....	\$2,810,304	\$2,527,145
Uncollected cash items .....	634,903	631,426
Bank premises .....	2,359	2,433
All other assets .....	257,666	98,935
Total assets .....	\$4,239,455	\$3,979,079
<b>LIABILITIES</b>		
Federal Reserve notes .....	\$2,615,923	\$2,444,268
Deposits:		
Member bank reserve accounts .....	991,103	853,005
United States Government .....	522	76,536
Foreign .....	11,660	7,280
Other deposits .....	13,321	26,460
Total deposits .....	\$1,016,606	\$ 963,281
Deferred availability cash items .....	520,863	493,311
All other liabilities .....	20,499	14,568
Total liabilities .....	\$4,773,891	\$3,915,428
<b>CAPITAL ACCOUNTS</b>		
Capital paid in .....	\$ 32,782	\$ 31,826
Surplus .....	32,782	31,826
Total liabilities and capital accounts .....	\$4,239,455	\$3,979,079
Ratio of gold certificate reserve to Federal Reserve note liability .....	18.9%	27.1%

**EARNINGS AND EXPENSES**  
**Federal Reserve Bank of Philadelphia**

(000's omitted)	1968	1967
<b>Earnings from:</b>		
United States Government securities . . . . .	\$136,300	\$110,223
Other sources . . . . .	4,604	1,440
Total current earnings . . . . .	\$140,904	\$111,663
<b>Net expenses:</b>		
Operating expenses* . . . . .	9,584	8,742
Cost of Federal Reserve currency . . . . .	1,385	1,016
Assessment for expenses of Board of Governors . . . . .	750	567
Total net expenses . . . . .	\$ 11,719	\$ 10,325
Current net earnings . . . . .	129,185	101,338
<b>Additions to current net earnings:</b>		
Profit on sales of U.S. Government securities (net) . . . . .	41	40
All other . . . . .	427	77
Total additions . . . . .	\$ 468	\$ 117
<b>Deductions from current net earnings:</b>		
Loss on sales of U.S. Government securities (net) . . . . .	—	—
Miscellaneous non-operating expenses . . . . .	9	2
Total deductions . . . . .	\$ 9	\$ 2
Net additions . . . . .	459	115
Net earnings before payments to U.S. Treasury . . . . .	\$129,644	\$101,453
Dividends paid . . . . .	\$ 1,934	\$ 1,854
Paid to U.S. Treasury (interest on Federal Reserve notes)	126,754	97,703
Transferred to or deducted from (—) Surplus . . . . .	\$ 956	\$ 1,896

\* After deducting reimbursable or recoverable expenses.

## VOLUME OF OPERATIONS

### Federal Reserve Bank of Philadelphia

Number of pieces (000's omitted)	1968	1967	1966
<b>Collections:</b>			
Ordinary checks*	324,500	283,400	276,600
Government checks (paper and card)	32,800	32,700	30,800
Postal money orders (card)	14,600	17,300	18,200
Non-cash items	832	846	832
Food stamps redeemed	22,633	17,391	9,766
Clearing operations in connection with direct sendings and wire and group clearing plans**	655	706	697
Transfers of funds	271	248	233
Currency counted	319,700	305,200	297,500
Coins counted	492,377	560,700	403,800
Discounts and advances to member banks	(a)	(a)	1
Depository receipts for withheld taxes	1,056	799	662
Postal receipts (remittances)	271	282	280
<b>Fiscal agency activities:</b>			
Marketable securities delivered or redeemed	482	536	621
Computerized marketable securities (Book entry transactions)	13	—	—
Savings bonds and notes (F.R. Bank and agents)			
—Issues (including reissues)	10,506	9,934	9,512
Redemptions		7,260	6,993
Coupons redeemed (Government and agencies)		1,070	1,072
<b>Dollar amounts (000,000's omitted)</b>			
<b>Collections:</b>			
Ordinary checks	\$100,774	\$ 94,422	\$ 88,836
Government checks (paper and card)	8,952	7,983	6,993
Postal money orders (card)	253	248	254
Non-cash items	1,258	1,104	827
Food stamps redeemed	31	23	13
Clearing operations in connection with direct sendings and wire and group clearing plans**	61,742	54,568	49,908
Transfers of funds	250,695	219,815	192,718
Currency counted	2,351	2,258	2,205
Coins counted	58	63	45
Discounts and advances to member banks	1,193	323	1,806
Depository receipts for withheld taxes	5,695	3,935	3,348
Postal receipts (remittances)	1,008	929	914
<b>Fiscal agency activities:</b>			
Marketable securities delivered or redeemed	14,091	13,571	14,913
Computerized marketable securities (Book entry transactions)	7,877	—	—
Savings bonds and notes (F.R. Bank and agents)			
—Issues (including reissues)	468	459	464
Redemptions	403	385	381
Coupons redeemed (Government and agencies)	394	435	342

\* Checks handled in sealed packages counted as units.

\*\* Debit and credit items

(a) Less than 1,000 rounded.