OBJECTIVES OF FEDERAL RESERVE POLICY

1. Lecture given at our Research Seminar, Board Room, on May 11, 1967.

2. Presented to our Directors on June 1, 1967.

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Federal Reserve Bank of St. Louis

Material presented by President Bopp
Research Seminar
Federal Reserve Bank of Philadelphia
Thursday, May 11, 1967

OBJECTIVES AND RELATED PROGRAMS

Objective	Conditions Calling for or permitting an easing of credit	Conditions Calling for or permitting a tightening of credit
1. Full employment.........	Less than full employment.	Jobs in excess of workers.
2. Stable price level......	Declining prices.	Rising prices.
3. Convertibility of the currency..............	High and/or rising primary international reserves.	Low and/or declining primary international reserves.
4. Adequate growth.........	When growth is inadequate.	When growth is too rapid to be sustained.
5. A fixed rate of interest	When savings are inadequate.	When savings are excessive.
6. Productive credit.......	Increase in monetary volume of output.	Decrease in monetary volume of output.

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Material presented by President Bopp at the Stated Meeting of the Board of Directors of the Federal Reserve Bank of Philadelphia on Thursday, June 1, 1967.

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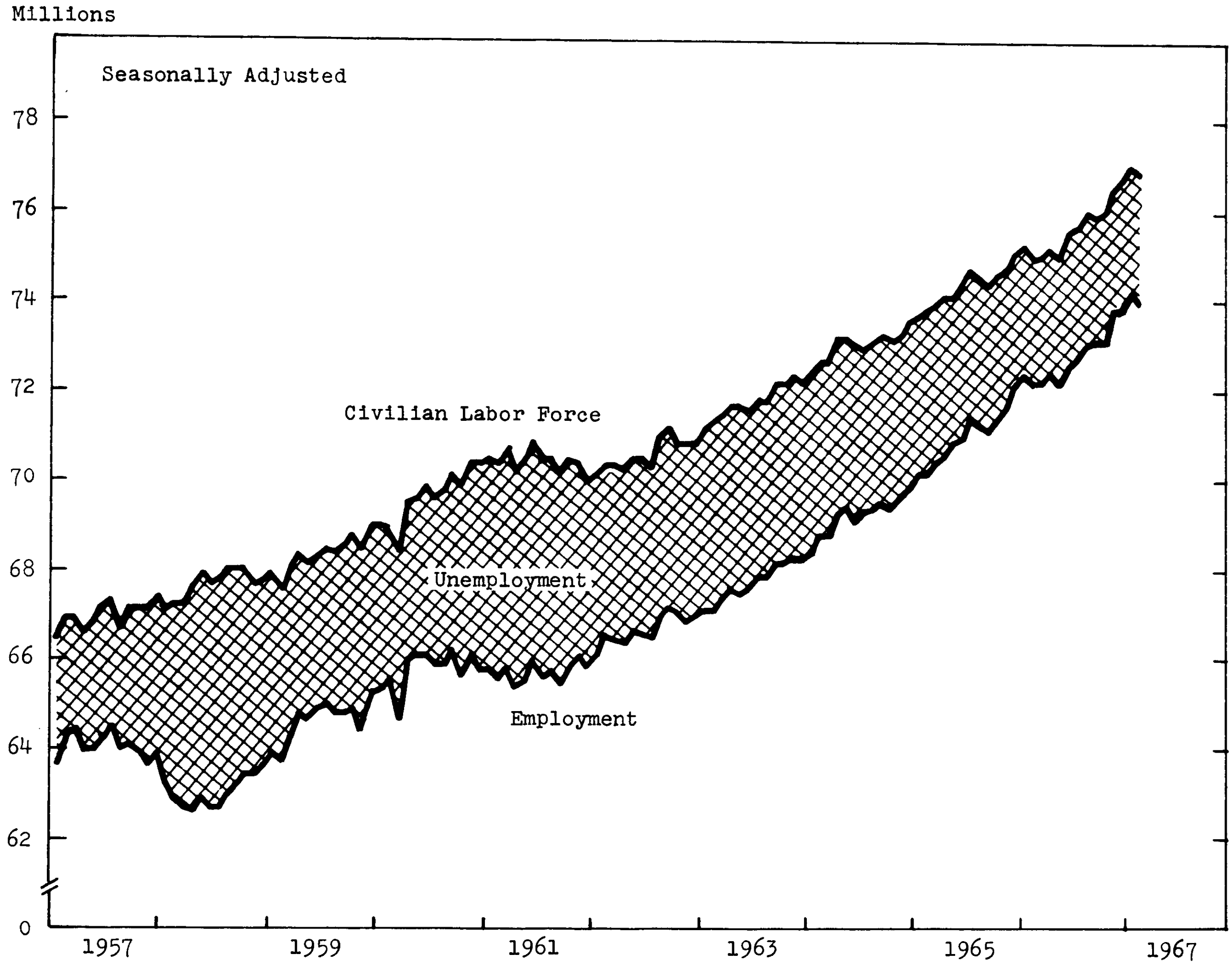
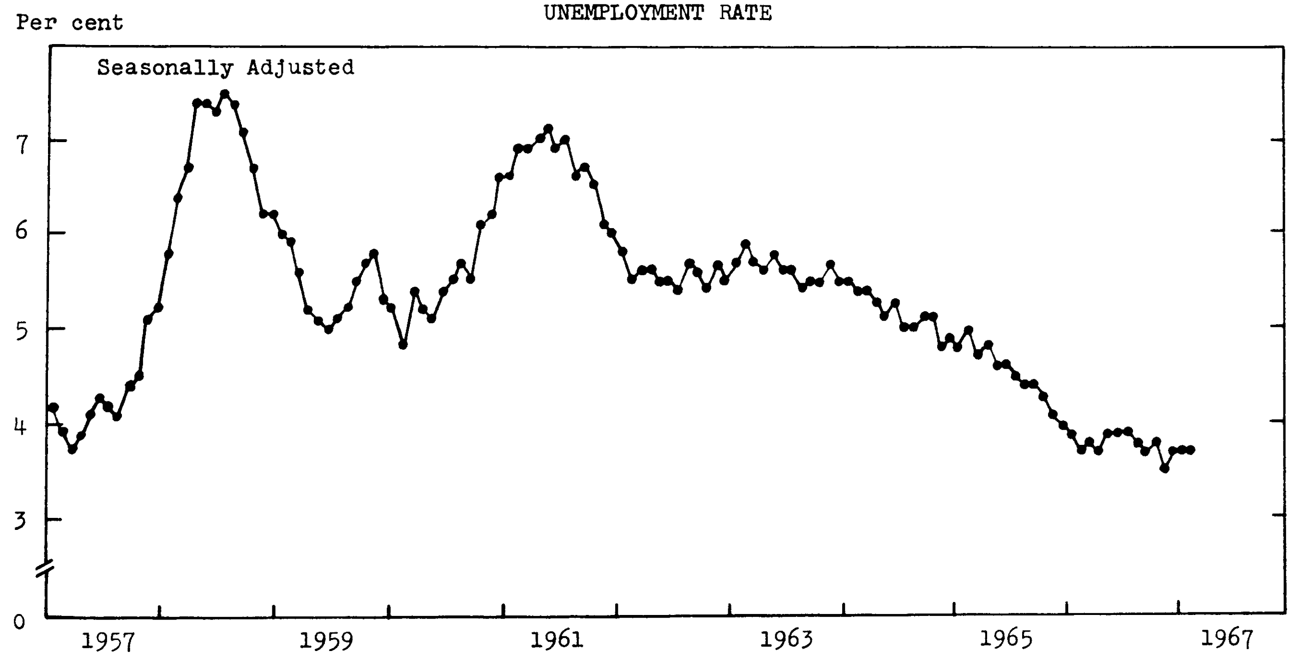
CIVILIAN LABOR FORCE AND EMPLOYMENT



UNEMPLOYMENT RATE



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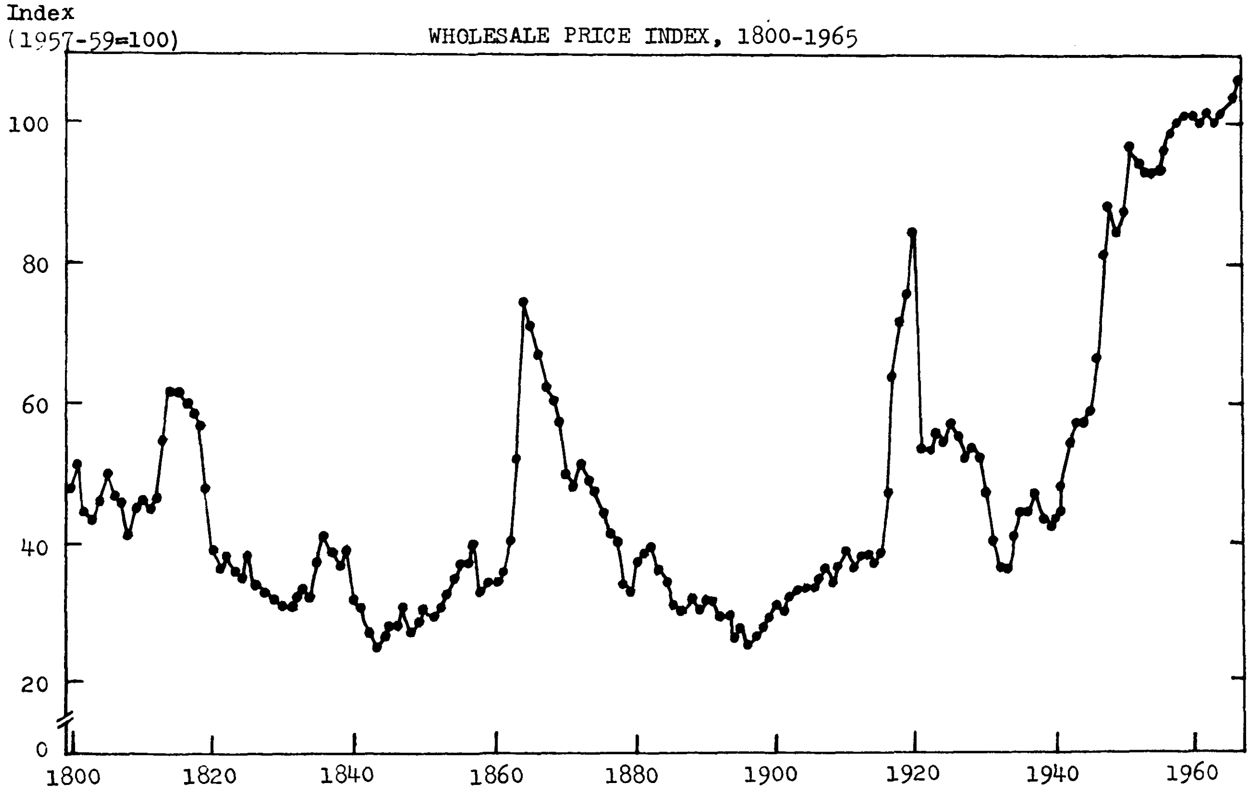
WHOLESALE PRICE INDEX, 1800-1965



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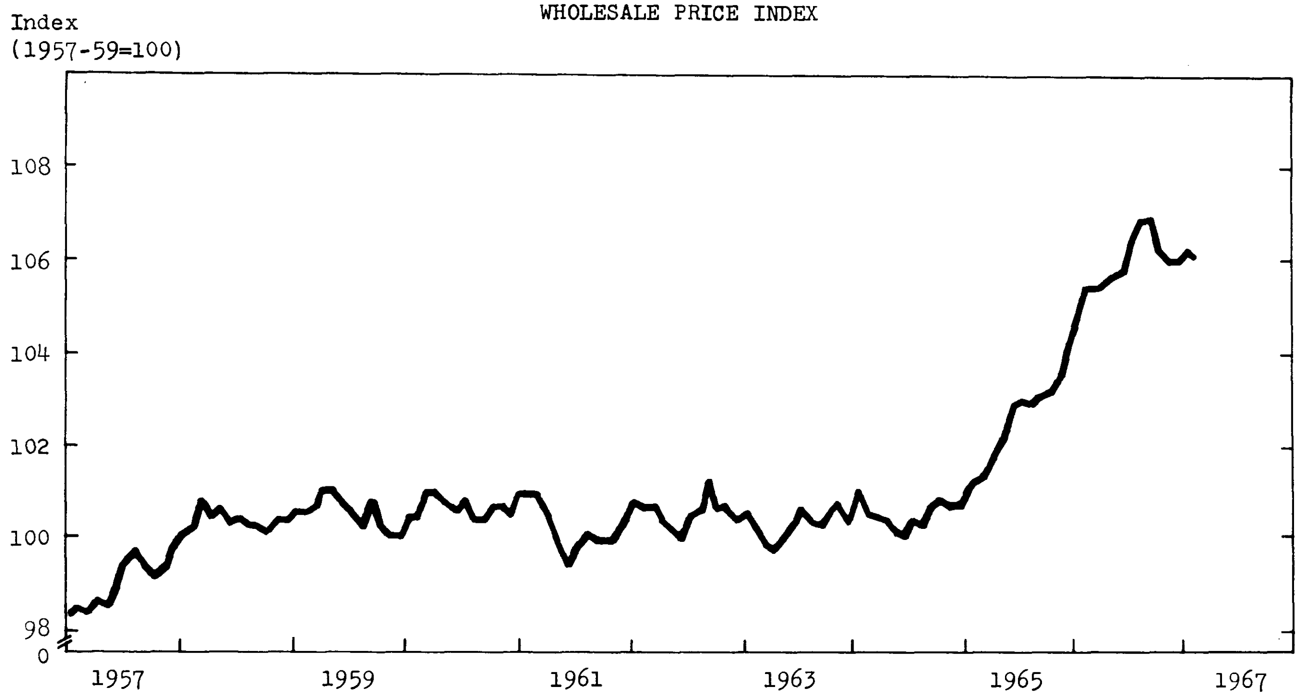
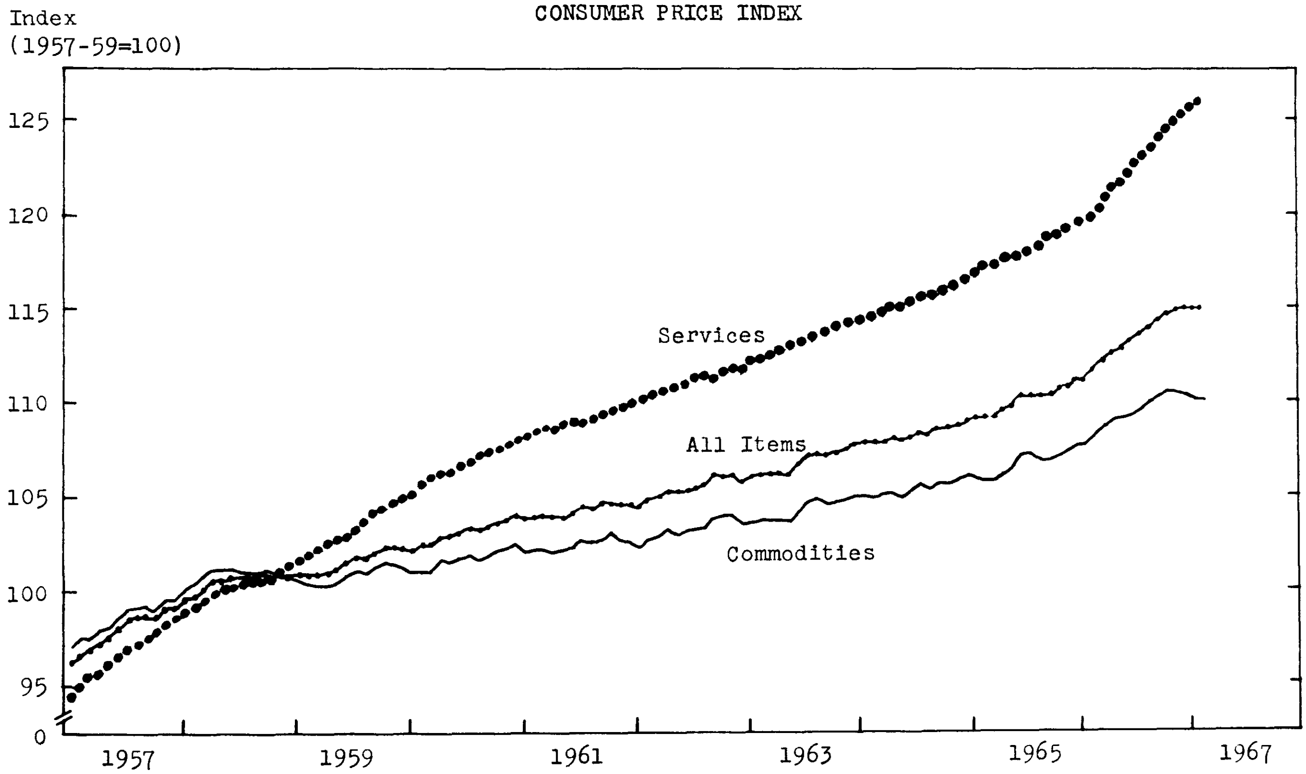
WHOLESALE PRICE INDEX



CONSUMER PRICE INDEX



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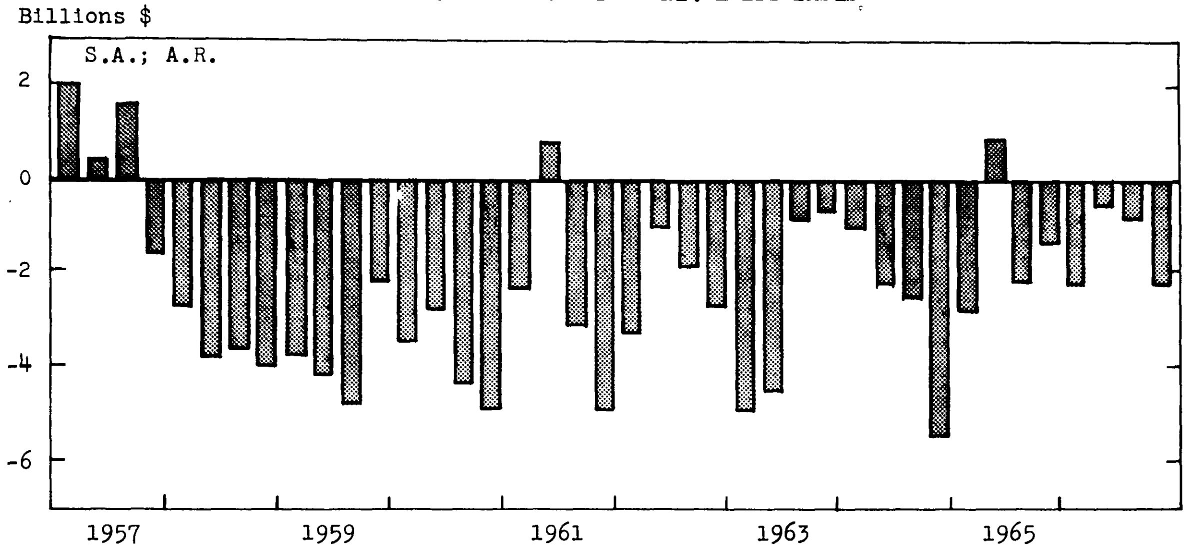
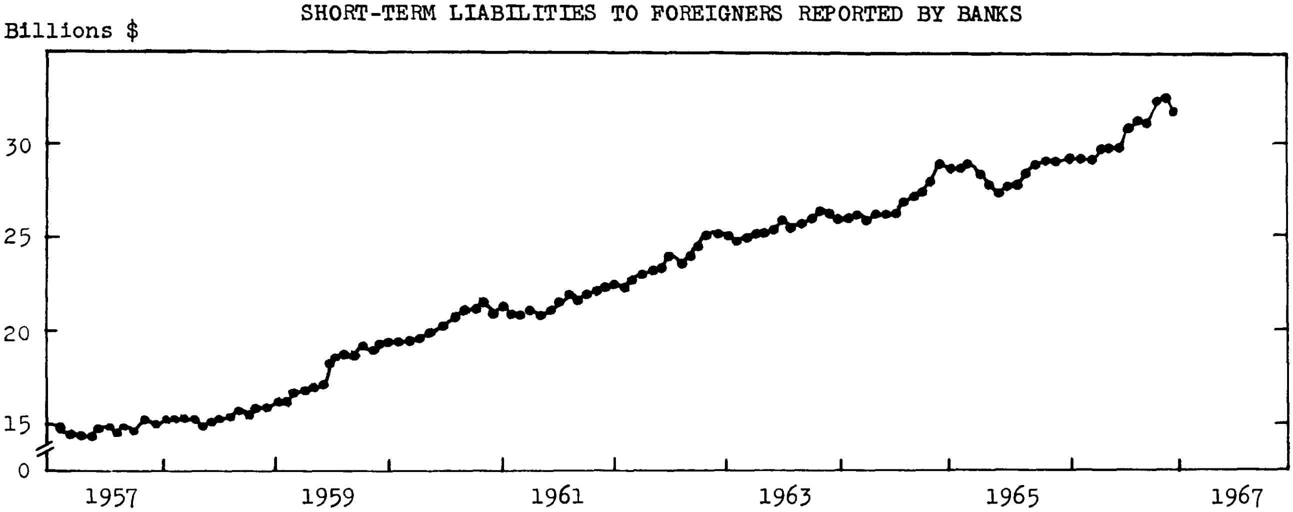
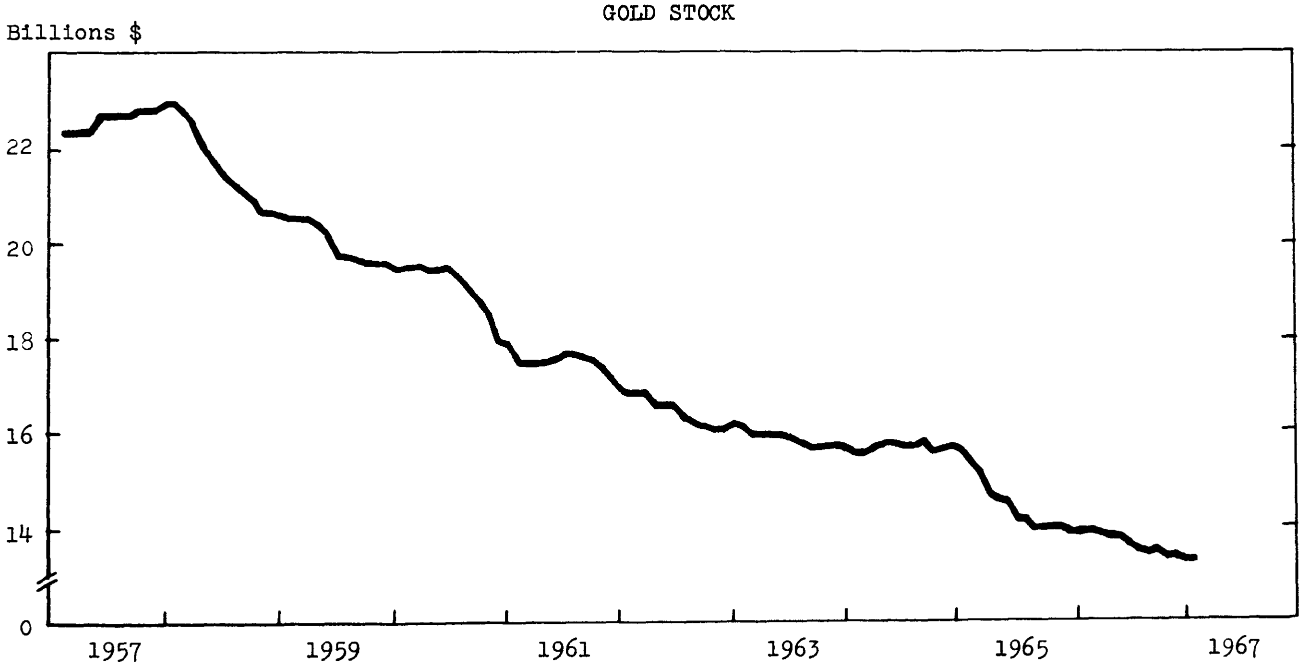
BALANCE OF PAYMENTS - LIQUIDITY BASIS



SHORT-TERM LIABILITIES TO FOREIGNERS REPORTED BY BANKS



GOLD STOCK



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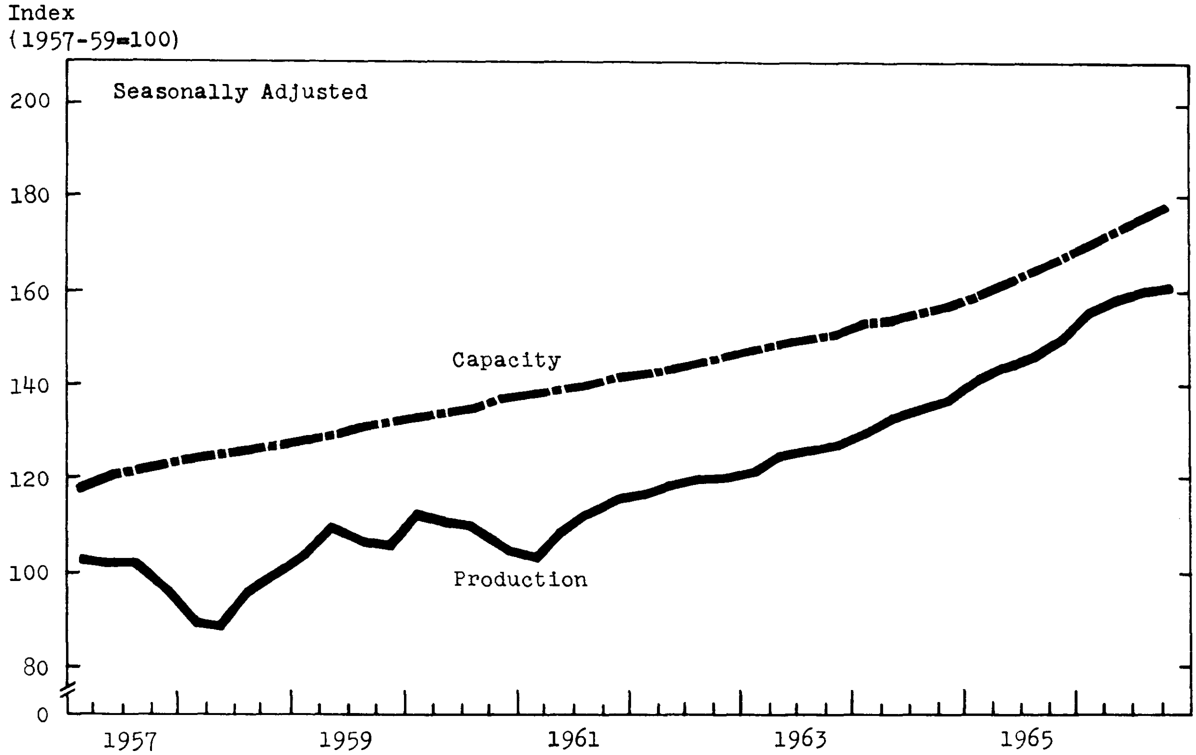
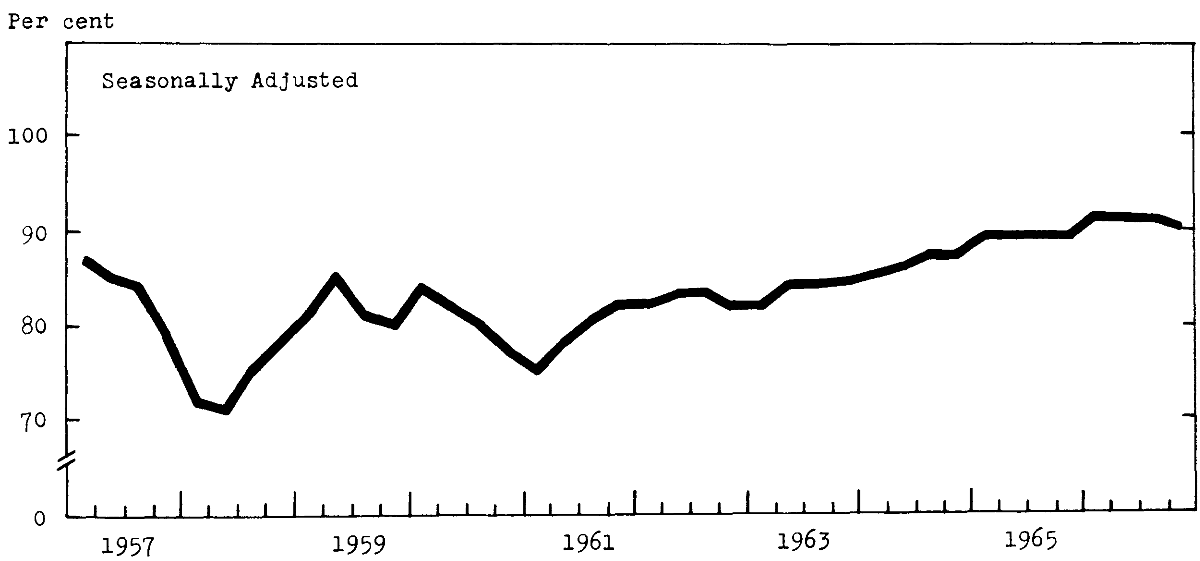
MANUFACTURING CAPACITY AND PRODUCTION



MANUFACTURING CAPACITY UTILIZATION



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(Excerpts from remarks made by President Bopp at the meeting of the Board of Directors of the Federal Reserve Bank of Philadelphia on Thursday, June 1, 1967.)

CONVERTIBILITY

For the United States convertibility still means redemption of currency in gold at a fixed price. Since this objective, more than any other perhaps, arouses great emotions, it might be worth-while to see how England came to adopt the gold standard in the first place.

Macaulay wrote: "In the autumn of 1695, it could hardly be said that the country possessed, for practical purposes, any measure of value of commodities. It was a mere chance whether what was called a shilling, was really tenpence, sixpence, or a groat." For example, the exchequer found that coins which should have weighed 220,000 ounces actually weighed only 114,000 ounces.

William and Mary appointed a committee to make recommendations for solving the problems. The membership was quite extraordinary: Sir Isaac Newton, Master of the Mint, John Locke, the great philosopher, and Lord Somers.

Sir Isaac recommended that the government call in the old coin at face value and issue new full weight coins. The ratio of silver to gold was established at 16 silver to 1 gold (shades of Bryan!). In major countries on the Continent the ratio was $15\frac{1}{2}$ to 1. Sir Thomas Gresham could have predicted the results a century before! Relatively, England overvalued gold and the Continent overvalued silver. Gold was taken to England for exchange into silver, which was taken to the Continent for exchange into gold, which . . . . Newton later recognized his error and recommended that it be corrected, but this latter advice was not followed[1/].

1/ This is the story as told by George F. Warren and Frank A. Pearson in their PRICES, New York, 1933, p. 159.

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A century passes and England is once again involved in war with her old enemy, France; this time under Napoleon. She abandons redemption of the currency but decides to resume convertibility after the war. The mint, of course, had very little silver to coin and Lord Liverpool decided to close it to the free coinage of silver because England was "naturally a gold country" and that "gold was the natural currency of England." And, indeed, it was if one admits, as he should, that it is only "natural" for even a Sir Isaac to make a mistake and for this mistake to have "natural" consequences.

It is irrelevant but tempting to speculate what might have happened if Sir Isaac had made a mistake in the other direction, say by adopting a ratio of 15 to 1. England might well have become "naturally a silver country." With the role that sterling acquired on the basis of English leadership in industry and commerce throughout the world, who knows, the world might naturally have been on the silver standard.

These are irreverent conjectures. Still, the faithful have propagated some fictional natural history. One gains an impression that the gold standard existed for centuries without interruption. Yet it has not existed in modern times for as long as a century, though England almost made it from 1822 to 1914.

My own view is that England arrived on the gold standard because of a mistake by Sir Isaac Newton in 1696. The gold standard survived the nineteenth century only because of the miracles of new gold discoveries in the 1840's and 1890's. Finally, when one sees the incredibly small amount of gold frequently held by the Bank of England, he is forced to conclude it was not a self-regulating system but was in fact maintained through management by the Bank of England. Thus, a mistake, miracles, and management describe the System more accurately than does a mystical natural providence.

Do not misunderstand me. I think that on balance an international

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monetary system -- essentially this means a system of relatively fixed rates of exchange -- is preferable to a system of national currencies with freely fluctuating rates, despite its presumed intellectual attractions.

An international system, however, requires genuine international cooperation on the part of the members based on rational economic principles. Such a system should indeed put pressure on a member which has an unfavorable balance of payments because it has pursued policies of over-full employment and inflation. It should not, however, put pressure on a member that has an unfavorable balance of payments despite significant unemployment and stable or even falling prices.

As you know, negotiations are now in process to reform and supplement the international monetary system. Fortunately, we are not at the moment operating in a crisis atmosphere.

. . . . .

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