

Statement of Eliot J. Swan
President of the Federal Reserve Bank of San Francisco
San Francisco, California
before the
Joint Economic Committee
on
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I will not attempt to review the record of the economy in detail in 1962, since that has been done for you most capably by a number of others. I will offer some general observations in this regard, however, for what they may be worth.

Since early 1961, we have had a broadly based recovery, with remarkably few distortions. The economy absorbed without serious difficulty a sharp stock market decline earlier this year, took the Cuban crisis in stride, and shows little indication of unsustainable growth or speculative weaknesses in inventories or new plant and equipment, the principal areas of fluctuation in the past. The index of wholesale prices has been remarkably stable, the behavior of consumer prices not quite as satisfactory. At the same time, however, over-all growth has been disappointingly modest, the level of unemployment continues to be of real concern, and there seems to be no clear and imminent prospect of a significantly more rapid upward pace of business activity.

The other pressing problem that has persisted throughout the recovery is the deficit in our balance of payments. The improvement in 1962 over 1961 was disappointingly small, and there is clearly a considerable way yet to go to reach a satisfactory position.

Despite these serious and persistent problems, I believe monetary policy was reasonably satisfactory in 1962. Continued reserve availability resulted in a record increase in bank credit, longer term interest rates declined, in contrast to their behavior in other periods of rising activity,

and short-term rate levels, in combination with foreign currency operations of the Treasury and the Federal Reserve, helped to discourage outflows of short-term funds, whether for speculative reasons or because of interest rate differentials.

There are those who would say that the level of unemployment requires a much easier monetary policy, and there are those who would say that the balance of payments situation requires a much tighter monetary policy. I fear that I could not satisfy either group of critics under present circumstances, although I am fully aware that a significant decline in business activity--or a real loss of confidence in the dollar leading to a run to other currencies and gold--neither of which I hope will occur--might well raise considerations of a marked policy shift in the one direction or the other. While I do not believe developments so extreme in either direction are imminent, I do believe that either might well be encouraged by an arbitrary and abrupt switch in monetary policy at this time. At this point, shift to really tight money could place a road block in the upward path of the economy; a shift to substantially easier money could contribute to a loss of confidence in the dollar and to an exchange crisis. Under present conditions, I see no alternative to making haste slowly with monetary policy, frustrating as that may be to the impatient who hope for simple solutions to extremely complex problems.

In no sense am I decrying the importance of monetary policy. The wrong monetary policy can do incalculable harm, and the right monetary policy can help to provide a climate in which appropriate adjustments can take place. However, no monetary policy, can directly make or assure such

adjustments--nor should it so long as we depend on the greater share of our economic decisions taking place through market processes.

In my opinion, monetary policy has been easy in 1962. Time deposits increased markedly throughout the year, and demand deposits have risen significantly since August. Business spending, however, must be motivated by prospective profits, which result in large measure from market opportunities that can be developed from new processes at lower costs and new products. Some portion of our unemployment appears most unlikely to respond directly to increased demand. Job opportunities and unemployment unfortunately may be found together, as evidenced by the demands of defense related industries on the West Coast for skilled personnel, even though we have many people looking for jobs in the same areas.

Under present circumstances, relative price stability is doubly important; not only to discourage unsound and speculative developments in the domestic economy, but also to encourage our industries to become increasingly competitive throughout the world, if we are to increase exports further relative to imports. But again, the search for new markets in other countries and the development of products and marketing efforts that will expand markets abroad ~~is~~ essential. Many other factors in the balance of payments are also obviously outside of the realm of monetary policy. The need for greater sharing of military and foreign aid burdens by our allies, for lowering of barriers to our exports, and for removal of limitations in foreign capital markets are familiar problems to all of you.

Certainly, I share the compelling concern for economic growth. But growth that is not sustainable, growth that creates imbalances that

lead to severe readjustments and recession, growth that does not reflect the mix of goods and services desired by the American people, as expressed both in the market and collectively through the processes of government, is not an adequate answer.

In the monetary area, policy should basically be directed toward facilitating the flow of funds in the money and capital markets without inflation, and this is what the Federal Reserve is seeking to accomplish. In this connection, the question of the degree to which the prospective Federal deficit should be financed through the banking system, which has been given further currency by the proposed tax reductions, involves the difficulty of seeking an answer, in isolation, to a problem that cannot be isolated. I do not believe a categorical answer can be provided, since the problem is really the ever present one of the sources of funds to meet total credit demands, both public and private. This is a continuous process, involving a continuing judgment about the relation of bank credit expansion to the flow of saving and spending, the availability of labor and other productive resources, the behavior of the price level, and our international economic position.

Monetary policy can assist significantly in providing a climate or a setting favorable to balanced and sustainable economic growth, but such growth itself can only be the result of a complex of factors related to the whole range of private decisions and public policy.