liam McChesney Martin, Jr., Papers
26/Folder 1

Series V, Subseries D
Hearings, July 1960-June 1961

HEARINGS

(51) Joint Economic Committee,
Wright Patman, Chairman ..... President's Economic Report - 2:30 p.m. 3/7/61

(52) Joint Economic Committee,
Wright Patman, Chairman ...... Board's Annual Report (to review operations of the FRBoard and Federal Open Market Committee) Robert Rouse, a.m. of June 1; President Hayes, am of June 2............ 6/2/61

No prepared statement

Hearings
Continued in Folder 2, 1961

(51)

Martin Statement

JOINT ECONOMIC COMMITTEE

Wright Patman (Texas), Chairman
Paul H. Douglas (Illinois), Vice Chairman

John Sparkman (Ala.)
J. W. Fulbright (Ark.)
William Proxmire (Wis.)
Claiborne Pell (R.I.)
Prescott Bush (Conn.)
John Marshall Butler (Md.)
Jacob K. Javits (N.Y.)

Richard Bolling (Mo.)
Hale Boggs (La.)
Henry S. Reuss (Wis.)
Martha W. Griffiths (Mich.)
Thomas B. Curtis (Mo.)
Clarence E. Kilburn (N.Y.)
William B. Widnall (N.J.)

Ch. Martin

APR 7 1961

The Honorable William Proxmire,
United States Senate,
Washington 25, D. C.

Dear Senator Proxmire:

This is in reply to your letter of March 30, 1961, referring to my testimony before the Joint Economic Committee, on March 7, 1961, and my further statement on unemployment supplementing my testimony.

It was my intention in both instances to call attention to the dual nature of our current unemployment problem, arising as it does both from contraction of over-all demand and from changes in structural factors in the economy. I also suggested what I thought were the appropriate policies applicable to the differing causes of unemployment.

With respect to your observation of a "sharp and decisive contradiction" between Dr. Heller and me, it is my understanding that the Council of Economic Advisers, in emphasizing the importance of moving to combat cyclical unemployment, was not seeking to minimize the need for appropriate action to help relieve conditions arising from structural changes of the type to which I have referred, as I indicated in the statement supplementing my testimony. Indeed, the Council stated explicitly that such measures "should be high on the agenda of national policy."

A large body of information has been gathered in recent years by Congress, various Government officers, and private research organizations dealing with the amount, characteristics and persistence of structural unemployment. While there are differences in emphasis, the general consensus of these studies is that in recent years unemployment has been high and persistent even in periods of expanding activity. An important factor causing such chronic unemployment has been dynamic structural changes in the economy.

Within the past week, the National Planning Association has released an informative document entitled "The Rise of Chronic Unemployment". This report presents a very interesting statistical and interpretive analysis of the increase in structural unemployment in recent years. The National Planning Association also concludes, "However, even if in a cyclical upswing chronic unemployment becomes somewhat alleviated, this does not mean that its causes are being removed. It is a sobering fact that the recovery periods over the last ten years, far from solving the problems of chronic or structural unemployment, have mainly succeeded in masking its extent and seriousness. Therefore, it is necessary to face up to the fact that the persistence of chronic unemployment presents us with a specific problem and separate measures to combat it will have to be devised in addition to the pursuit of anti-cyclical policies and those designed to support economic growth."

My response to your question as to an acceptable level of unemployment and goals must be the same as I have made many times to the Joint Economic Committee. The System has long recognized that no single index or simple combination of indicators can serve as a continuing infallible guide to its policy. The goals and the guides of credit and monetary policy must be broad and adaptable to changing times and conditions. However formulated, their pursuit inevitably requires discretion, patience, and skillful judgment in the light of the fullest and widest information available respecting the credit situation and indeed all phases of the national economy. Moreover, their success will be conditioned by various other policies, programs, and activities of Government, by a wide range of private activities, and by the changing moods and impulses of businesses and the public generally with respect to spending, borrowing, and saving.

In answer to your last question I would say that the implicit predominant purpose of the Federal Reserve Board is to contribute, insofar as the limitations of monetary and credit policy permit, to an economic environment favorable to sustained economic growth and the optimum utilization of our expanding industrial and manpower resources. Traditionally this overall policy has been followed by easing credit conditions when deflationary factors prevailed and, conversely, by restrictive measures only when inflationary forces threatened.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

MW:mas

LIAM PROXMIRE
WISCONSIN

United States Senate

WASHINGTON, D. C.

March 30, 1961

Honorable William McChesney Martin
Chairman, Board of Governors
Federal Reserve System
Washington, D. C.

Dear Chairman Martin:

Your further statement on unemployment, supplementing your testimony to the Joint Economic Committee, on March 7, 1961, reached me this morning. While I appreciate having these additional comments on the nature of unemployment in the American economy today, it does seem to me that you have failed to come to grips with the salient points raised by the differences between your original testimony and that of Dr. Heller.

As you will recall, I initiated the questioning of those differences during the hearing on March 7. Subsequently, on March 9, I discussed them on the floor of the Senate. I observed that the difference between your testimony and that of Dr. Heller amounts to a sharp and decisive contradiction of economic policy. I inserted a brief analysis of the specific differences at the close of my remarks. An excerpt from the Record for March 9 is attached for your convenience.

Your further statement now comments generally on the problem of unemployment without offering any further, deeper analysis of the questions raised by the conflicts between your earlier remarks and those of Dr. Heller. As you know, Dr. Heller attached an appendix to his main statement which specifically challenged the view that unemployment at present is so substantially structural in nature that anti-cyclical programs would soon be seriously inflationary. He provided statistical tables showing for example, a remarkably uniform increase in unemployment between 1957 and 1960 in a number of industries regardless of their structure or technology. Since you provide no similar statistical support for your position, I would very much appreciate having a detailed, statistical analysis from you which would support your contentions.

To the crucial question of what would constitute an "acceptable" level of unemployment, Dr. Heller gave a specific answer. He stated that 4% unemployment would be the level the economy should attain before policies of contraction, i. e., diminution in money supply relative to GNP, or hiking taxes, decreasing spending, should be adopted. I hope you will also give us your estimate of a satisfactory unemployment reduction "target", so that the Committee will have a benchmark against which to measure future monetary and fiscal policies.

If you should feel that this should be a matter of balancing a number of criteria such as profits, retail sales, prices, gold outflow, as well as unemployment, please indicate as precisely as possible how significant an upward movement in these criteria would be necessary to suggest government policies of contraction at 6%, 5%, 4% unemployment.

For example, would you agree that governmental action to contract its effects on the economy would be inappropriate when unemployment is above 4%, provided the price level is stable or falling and the international payments picture is not strongly unfavorable?

Sincerely,

Bill Proxmire

William Proxmire, U. S. S.

Enclosure

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Attached statement submitted for the transcript of Mr. Martin's testimony before Joint Economic Committee on the President's Economic Report--in response to a request by Representative Curtis.

STATEMENT OF THE BOARD'S VIEWS ON OECD

In the modern world of interdependent nations, suitable international forums in which economic questions of mutual interest can be considered and discussed have an important role to play. In the postwar period the Organization for European Economic Cooperation has provided one such forum for its member countries in Western Europe, and for Canada and the United States, which have been associate members. The proposal to reconstitute the OEEC as the Organization for European Economic Cooperation and Development (OECD) results from the great change in economic conditions and economic problems in the past decade, and particularly from the re-establishment of world multilateral trade and the convertibility of most leading currencies. In addition to its other activities, the OECD would provide the basis for continuation and intensification of international economic consultation and cooperation among the countries concerned. Member countries would thus be provided with an opportunity to inform themselves more fully than might otherwise be possible regarding the policies of their fellow members, and to express their views regarding the consonance of such policies with their own economic interests.

It must be remembered, of course, that there are practical limits on the extent to which it is possible to reconcile the economic policies of different countries. These limits result from the variation among their economic conditions, among their techniques of economic control, and, at times, among their views as to what policies are suitable in particular circumstances. On various occasions, representatives of the United States in Paris negotiations have pointed out the existence of such limits, and the Board of Governors fully agrees with this view.

The Board of Governors understands that nothing in the Convention embodying the proposed organization would affect the present status of the Federal Reserve System in the structure of the U. S. Government or its independence of judgment and action in the field of monetary policy.

March 9, 1961

TO: Board of Governors

FROM: Ralph A. Young

In his testimony on Tuesday, Chairman Martin was asked by Representative Curtis whether the Board had made anywhere a statement of views concerning the OECD Treaty. After eliciting Mr. Martin's views, Representative Curtis further requested that the "Federal Reserve have a statement, a considered statement, for insertion in the record as to your position on OECD as you have expressed it, that you do not feel that this would in any way affect your independent judgment and powers that you presently have."

To respond to this request, there is attached a suggested draft statement for the Board's consideration. Also attached is the excerpt from the testimony covering Representative Curtis' colloquy with Chairman Martin.

Attachments 2

DRAFT STATEMENT OF THE BOARD'S VIEWS ON OECD

In the modern world of interdependent nations, suitable international forums in which economic questions of mutual interest can be considered and discussed have an important role to play. In the postwar period the Organization for European Economic Cooperation has provided one such forum for its member countries in Western Europe, and for Canada and the United States, which have been associate members. The proposal to reconstitute the OEEC as the Organization for European Economic Cooperation and Development (OECD) results from the great change in economic conditions and economic problems in the past decade, and particularly from the re-establishment of world multilateral trade and the convertibility of most leading currencies. In addition to its other activities, the OECD would provide the basis for continuation and intensification of international economic consultation and cooperation among the countries concerned. Member countries would thus be provided with an opportunity to inform themselves more fully than might otherwise be possible regarding the policies of their fellow members, and to express their views regarding the consonance of such policies with their own economic interests.

It must be remembered, of course, that there are practical limits on the extent to which it is possible to reconcile the economic policies of different countries. These limits result from the variation among their economic conditions, among their techniques of economic control, and, at times, among their views as to what policies are suitable in particular circumstances. On various occasions, representatives of the United States in Paris negotiations have pointed out the existence of such limits, and the Board of Governors fully agrees with this view.

The Board of Governors understands that nothing in the Treaty embodying the proposed organization confers any power to bind the United States without compliance with applicable procedures imposed by domestic law. On this basis, it is clear that neither the present status of the Federal Reserve System in the structure of the U. S. Government nor its independence of judgment and action in the field of monetary policy would be affected by U. S. membership in the OECD.

EXCERPTS FROM CHAIRMAN MARTIN'S TESTIMONY ON MARCH 7, 1961, BEFORE JOINT ECONOMIC COMMITTEE CONCERNING OECD

(From unedited transcript of hearing)

"Representative Curtis. * * *

"The question I would like to ask, though, is whether the Federal Reserve has made a statement in regard to its position or where it is going to be in the event of the OECD Treaty being adopted.

"First of all, has a statement been made, issued by the Federal Reserve on your position?

"Mr. Martin. No, no statement has been issued by the Federal. I think that I have discussed it with Secretary Dillon on occasion, and as I understand it, the OECD set up is not decision-making.

"Representative Curtis. So you do not think it will be in any way adversely affect?

"Mr. Martin. I am assured that it will not, and certainly we are all in favor of the general cooperation which is involved in it. There are obviously complications in it because different central banks have different relationships to the Treasury, and if you are going to have a cooperative grouping of them, why you have the same problems that we have on interest rates that we are going to have the same interest rates we have to recognize that there are budgetary problems, fiscal and debt management problems and problems on the wage productivity aspect that would all have to be measured together also."

* * * * * *

"Representative Curtis. Mr. Martin, I wanted to get back to the OECD a little bit.

"Mr. Martin. Very well.

"Representative Curtis. I will read a passage in an article appearing in Commercial and Financial Chronicle of Thursday, February 23, by Herbert Bratter:

'One of the principal arguments advanced by Secretary Dillon for our ratification of the OECD convention is that OECD will bring about coordination of the monetary and credit policies of its members and make it possible to avoid such developments as our capital and gold outflow last year.

'The policies of the twenty central banks of the OECD countries will be coordinated. Our Federal Reserve Board, for example, will keep in close and more or less continuous contacts in OECD with the central banks of Britain, Canada, and Continental countries, and vice versa, before instituting policies which, whatever their validity for domestic purposes, may have undesirable effects on other OECD countries'.

"The only reason I read that is the request that I was going to make to the Chairman.

"Would the Federal Reserve have a statement, a considered statement, for insertion in the record as to your position on OECD as you have expressed it, that you do not feel that this would in any way affect your independent judgment and powers that you presently have.

"I cannot believe it would, myself, in this treaty, but I think it is a very important thing, particularly as the Federal Reserve has not commented.

"That was my first question.

"You have not made an official statement on it. Would you care to do that and would you prepare a statement for us.

"Mr. Martin. I will be very glad to, Congressman Curtis."

87TH CONGRESS 1st Session } SENATE { EXECUTIVE REPORT No. 1

ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT

REPORT

OF THE

COMMITTEE ON FOREIGN RELATIONS
UNITED STATES SENATE

ON

EXECUTIVE E, 87TH CONGRESS, 1ST SESSION

MARCH 8, 1961.—Ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE
57119 WASHINGTON : 1961

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CONTENTS

87TH CONGRESS } SENATE { EXECUTIVE REPT.
1st Session } { No. 1

ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT

MARCH 8, 1961.—Ordered to be printed

Mr. FULBRIGHT, from the Committee on Foreign Relations, submitted the following

REPORT

[To accompany Ex. E, 87th Cong., 1st sess.]

The Committee on Foreign Relations, having had under consideration the Convention on the Organization for Economic Cooperation and Development, together with two protocols relating thereto, signed at Paris on December 14, 1960 (Ex. E, 87th Cong., 1st sess.), reports the convention and protocols to the Senate and recommends that the Senate give its advice and consent to ratification.

PURPOSE AND BACKGROUND OF THE CONVENTION

Since the end of World War II, vast changes have swiftly transformed relations between the non-Communist industrial nations, as well as relations between these powers and the less developed but politically awakened areas of the world. The Organization for Economic Cooperation and Development (OECD) reflects these changes, and has been designed to cope with those that can determine economic stability and growth.

Structurally, the OECD consists of the 18 European members that comprised the OEEC (Organization for European Economic Cooperation), plus the United States and Canada. The OEEC was established in 1948 to help Europe recover from the war. It recommended allocations of Marshall Plan aid to member countries, established the European Payments Union and liberalized intra-European trade. The OECD amounts to a recognition that the objective of the predecessor organization has been attained, and has given way to another and equally urgent set of problems that can be adequately dealt with only by a remodeled organization, in which the United States and Canada are participants.

The OECD has two broad purposes. One is to promote economic stability and the orderly growth of the economies of member countries. The other is to devise more effective methods of assisting the less developed countries, and for arranging to distribute the aid burden more equitably. Thus, on the one hand, the OECD reflects the growing interdependence of the economies of its member countries. And, on the other, it acknowledges the urgent need to narrow the gap between the rich and the poor countries, yet in a form that will not tax the economic vitality of any one of its members.

The OECD concept—the need for such an institution—has been widely discussed here and abroad in recent years. In the fall of 1959, behind an American initiative, these discussions assumed an official character. Next, in December 1959, the heads of Government of the United States, France, Germany, and the United Kingdom, meeting in Paris, publicly recommended an intensive study of methods of promoting consultations on major economic problems. This was followed by a ministerial meeting of January 14, 1960, in which representatives of the 18 OEEC countries and the United States and Canada adopted a resolution establishing a group of 4 experts to determine means by which the 20 nations could improve their cooperation on economic problems and development assistance.

On April 7, 1960, the Group of Four published its report, which proposed that the OEEC be reconstituted as the OECD. On May 25, senior officials of the 20 nations presented their governments' views on the Group of Four report and established a Working Party to draw up a draft convention remodeling the OEEC and to begin reviewing the OEEC acts.

On July 23, a Ministerial Conference reviewed the status of the project and established a Preparatory Committee to complete the transformation of the OEEC into the OECD. The Committee's report was adopted at the Paris Ministerial Meeting of December 13, 1960, and the convention with related protocols was signed the next day by the representatives of the 20 governments.

SUBSTANCE OF THE CONVENTION

The OECD Convention consists of 21 articles and 2 related protocols. The aims of the organization, as well as the methods and provisions for achieving these aims, are set forth in articles 1–6. A comparison of these six articles with the OEEC Convention reveals the following: The objectives of the OECD are broader than those of the OEEC. But the obligations are fewer and considerably less demanding. The OECD Charter provides for consultation and voluntary cooperation. The OEEC embodied rules and obligations to which each of its members was bound. Although preoccupied at the start with the distribution of Marshall Plan funds, the OEEC became generally concerned with intra-European trade and payments problems. For example, the OEEC countries developed a code of liberalization, which removed quantitative restrictions on member imports within a system of reciprocal commitments. As a concession to the United States, the OEEC's Code of Trade Liberalization has been discarded in its entirety. For some members, this was a major—and painful—concession.

Many of OEEC's other codes and obligations have also been allowed to lapse. None of those that will be carried over will apply to the United States. However, the United States has agreed to certain recommendations of the OEEC. The terms of these recommendations do not obligate the United States, or other members, to courses of action. Appendix No. 1 to this report is a memorandum of understanding which formally commits the 18 OEEC members to vote in the OECD Council for adoption of those OEEC acts that have been recommended by the Preparatory Committee. However, the United States and Canada are not similarly bound. Under paragraph 2 of this memorandum, the United States and Canada shall be released from the commitment to vote in the OECD Council for adoption of any acts in this category if appropriate notification is given no later than 10 days after the deposit of either country's instrument of ratification. The act then becomes applicable to all the other members, but not to an abstainee.

The OECD's basic purposes—to promote orderly economic growth within its 20 member community, and to assist more effectively the less developed countries—is embodied in article 1. Under article 2, the members agree to pursue these aims by promoting the development and most efficient use of their economic, scientific, and technological resources.

They also agree, under article 2 (c), to—

> pursue policies designed to achieve economic growth and internal and external stability and to avoid developments which might endanger their economies or those of other countries.

This language clearly reflects the rapid and sweeping postwar changes that have inspired the creation of the OECD. It acknowledges the growing and relentless interdependence of the economies of the member countries. These economies have together become an elaborate skein, the threads of which are the payments balances and economic policies of the member countries (and others, like Japan). The process of reaction and adjustment between them is a constant rhythm. Ideally, this process should also provide equilibrium, just as the free gold standard was once supposed to provide automatic equilibrium. Unfortunately, the tangled skein of international economics lacks the element that would assure stability, or automatic equilibrium. The OECD, through its Economic Policy Committee, will provide advice and recommendations designed to protect each member from economic disequilibrium.

The Secretary of the Treasury, Mr. Dillon, in testifying before the Committee on Foreign Relations, illustrated the need for the OECD mechanism with this reference to the U.S. balance of payments difficulties of 1960.

> During the first half of 1960 our balance of payments deficit on an annual basis was \$2.9 billion—down markedly from the level of \$3.8 billion in 1959. Last spring our Federal Reserve discount rate was at 4 percent, the German Bundesbank rate was 4 percent, and the Bank of England rate was 5 percent. In other words, all those rates were close together. Then, as business began to slow in the United States, our Federal Reserve began to ease credit and reduced its rate first to 3½ percent, and later to 3 percent. Meanwhile the German Bundesbank, with its eye on the domestic boom in Germany, and with the objective of controlling inflation at home, increased its discount rate to 5 percent in June. The Bank of England promptly followed suit and upped its rate to 6 percent.

These actions brought about a sharp imbalance in short-term interest rates. The results were bad for all concerned. A flood of short-term funds left New York seeking the higher return in Frankfurt and London. This sharply increased our balance-of-payments deficit from an annual rate of $2.9 billion in the first 6 months to a rate of $4.7 billion in the second 6 months. This sudden and sharp increase shook confidence in the dollar and the result was a substantial increase in the outflow of gold. This, in turn, brought on the speculative outbreak in the private gold market in London last October when for a day or two gold sold at $40 an ounce.

Meanwhile the large inflow of American funds frustrated the efforts of the German authorities to tighten up on investment in Germany. When this became clear, the German and British authorities both cut back their discount rates, the flow of short-term capital slowed and confidence was gradually restored.

The lesson to be learned by all this is that in these days of convertible currencies there must be close cooperation and coordination between our financial and monetary authorities and those of the major industrialized countries of Western Europe. This is now recognized on all sides. The OECD is the forum in which this coordination can be worked out and through which we can avoid similar episodes in the future. As such, it is a vitally important element in our drive to right our payments deficit without infringing on the actions that must be taken to reinvigorate our economy here at home.

Development Assistance Committee.—Under article 2(e), the OECD members have agreed to meet their development assistance responsibilities by providing capital and technical assistance to the less developed countries, as well as helping them to secure and expand export markets. The OECD instrument for this activity will be its Development Assistance Committee, successor to the Development Assistance Group, which operated throughout 1960 on an interim basis. Appendix No. 2 to this report is a breakdown of official assistance provided by the OECD members and Japan to less developed countries. It should be noted that the French figures include assistance to Algeria, which in the past has been regarded by French governments as part of Metropolitan France.

The Development Assistance Committee (DAC) initially will consist of nine OECD members—Belgium, Canada, France, Germany, Italy, the Netherlands, Portugal, the United Kingdom, and the United States—and also Japan. The DAC will not of itself be an operating, or "burden sharing," agency. Instead it will review aid programs, recommend levels and kinds of aid, as well as more efficient and equitable aid programming. It will be a clearinghouse for information concerning the needs of the less developed areas and a forum in which the capacities of the major industrialized nations of the West, along with Japan, can be measured against these needs. The DAC will thus enable nations which are meeting their responsibilities in this area to encourage laggard nations to assume their share of the burden.

Trade provisions.—Articles 1(c) and 2(d) provide that the OECD members will "pursue their efforts" to expand world trade "on a multilateral, non-discriminatory basis in accordance with international obligations"; also to try to "reduce or abolish obstacles to the exchange of goods and services * * *." The OECD's concern will be the broad outlines of trade policy, not tariff negotiations, or trade rules. These matters are the concern of the GATT (General Agreement on Tariffs and Trade) of which all OECD members, excepting Iceland, are contracting parties. Congress has never approved the GATT, and approval of the OECD will not constitute approval of the GATT. Articles 1(c) and 2(d) do not obligate members to take any actions which they otherwise would not take. These articles do mean that the OECD, as an extension of its function of providing economic stability, will become a consultative forum in which members can deal with general trade problems of concern to some or all of them.

As an example, Western Europe has divided into two trade blocs. Leaving aside the unproductive competition inherent in such a division, other problems appear. On January 1, 1961, the Common Market "Six" scaled down its internal tariffs on industrial items and some agricultural goods. The effect of these first adjustments has created some discrimination against imports from countries outside the "Six." Obviously, the United States and others must encourage the "Six" and the "Seven" (European Free Trade Association) countries to adjust their general trade policies in a way that will avoid further discrimination against those who are members of neither bloc. The OECD will be a forum for such discussions, as well as for the larger question of ending the trade division in Europe in a manner that will protect every country's interests. The problem affects the rich and poor alike.

In Africa, those countries which formerly were French colonies have the privilege of association with the "Six." This means that they can—and do—sell their goods in a preferred market. It also means that neighboring African States—Nigeria, for example, which in 1959 sold 35 percent of its exports to the "Six"—must compete for this market against a rising tariff wall. Appendix No. 3 to this report contains two tables, (*a*) and (*b*), which show respectively the importance of OECD countries as a market for the less developed countries; and the proportion of export earnings of selected less developed countries derived from their primary products.

In article 2(d), one of the two trade provisions, the members also agree to try to "maintain and extend the liberalisation of capital movements." At present, only Belgium-Luxembourg, Canada, the United States, and Germany, among the members, permit the unrestricted flow of capital from their countries. This is another example of a problem that can be discussed within the broad, multilateral framework of the OECD.

Other provisions.—In article 3 the members agree (a) to "keep each other informed"; (b) to "consult together on a continuing basis"; and (c) to "co-operate closely and where appropriate take co-ordinated action."

The language "where appropriate" makes article 3(c) permissive rather than mandatory. Furthermore, article 6(3) provides that—

> No decision shall be binding on any Member until it has complied with the requirements of its own constitutional procedures. The other Members may agree that such a decision shall apply provisionally to them.

Articles 7–14 are concerned with organization and procedural matters. Subsidiary bodies, such as the Economic Policy Committee and the DAC, would be established under the authority of article 9.

Article 15 concerns the status of OEEC acts that might be carried over. It provides that "* * * decisions, recommendations and resolutions of the Organization for European Economic Cooperation shall require approval of the Council to be effective after the coming into force of this Convention." Under article 6, each member shall have one vote on the Council, and "decisions shall be taken and recommendations shall be made by mutual agreement of all the Members."

Article 17 allows any member to terminate membership in the convention by giving 12 months' notice of that intention to the depositary government.

Articles 18–21 cover the location of the OECD Headquarters (Paris); budgetary procedure; and notification responsibilities of the depositary government.

Protocols.—There are two supplementary protocols to the convention. The first gives the members of the European Economic Community the option of acting individually within the OECD, or jointly through one of their commissions, such as the High Authority of the Coal and Steel Community, or the European Atomic Energy Community. The second protocol covers the privileges, exemptions, and immunities of OECD officials and representatives.

COMMITTEE ACTION

The convention, with related protocols, was transmitted to the Senate by President Eisenhower on January 17, 1961. On February 14 and 15, the Committee on Foreign Relations examined the convention in public session. Witnesses from the executive branch, representing President Kennedy, were heard on February 14. They were the Secretary of the Treasury and the Under Secretary of State for Economic Affairs. On February 15, the committee heard testimony from all other persons who had asked to appear.

The Chairman, Mr. Fulbright, asked whether article 6 (1) endowed the individual members with a veto power over the decisions and recommendations of the OECD Council. Under Secretary Ball, answering in the affirmative, said:

> A nation which opposes a particular proposal has the option either of voting against it, in which case the proposal is killed, or of abstaining, in which case the proposal does not apply to that country.

The chairman, in referring to Secretary Dillon's comment on the relationship between discount rates and capital outflows, asked whether the OECD's authority would "affect the power of the Federal Reserve Board to alter our discount rates." Secretary Dillon said no. Senator Morse carried the question a step further and asked whether the jurisdiction of the Federal Reserve Board might be enlarged by the creation of the OECD. Secretary Dillon replied:

> * * * this convention, will not in any way, shape or form enlarge the authorities of the Executive or of the Federal Reserve or any other organization in the U.S. Government to take actions which are not already provided for * * * under act of Congress.

OECD and GATT.—Senator Sparkman asked whether this organization would, or could, perform any of the functions that had been contemplated for the ITO (International Trade Organization), or whether the OECD bears any relationship to the GATT.

Secretary Dillon said that there is no connection whatsoever. He added that during the OECD discussions some of the countries objected to the elimination of the code of trade liberalization, because they felt they drew a measure of protection from these trade rules. However, the American position was accepted at the July OECD ministerial meeting. It was stated then by Secretary Dillon as follows:

> * * * In the [U.S.] Constitution it is * * * specified that foreign trade is within the competence of the Congress of the United States and not within the competence of the Executive. All the actions which the Executive takes in this field and has taken over the past years in the form of trade agreements and so forth have been taken on this specific authority which has been voted by the Congress of the United States through the original Trade Agreements Act and

its various extensions, the last of which occurred in 1958. It is impossible for the United States to agree to anything which would infringe this competence of the Congress.

One thing to which this happens to apply is the question of detailed and fixed procedures and rules which have to be approved by the Congress as part of our joining, working with, any new organization. We have suggested three times in the last 10 years to our Congress, once under the Democratic administration, and twice under the administration of President Eisenhower, that rules and procedures which had been worked out by experts, and which would help the functioning of the GATT, be specifically approved by the Congress. Three times the Congress has refused to do that, allowing us to continue to operate within the framework of the GATT, but saying that as a Congress they would not approve any specific rules which might have the effect of binding or making it more difficult for them to operate with freedom in the field of trade in the future. It is very clear that this same consideration applies to this Convention. Any attempt to tie in rules of trade, rules of procedure that are fixed and definite, would not be acceptable to our Congress and that is the reason why the United States Representatives have continually objected to such rules and regulations.

It is not a question of substance, the substance of whether we wish to talk about things or do not wish to, but it is a very important question of procedure and the prerogative of our Congress, which we are bound to uphold. It would be no use for us to reach an agreement around this table that we know would not be acceptable to our Congress, and would be doing a disservice to all of us sitting here. That is why I have dwelt on this problem.

Senator Aiken also sought a more precise understanding of the intent of articles 1(c) and 2(d), the trade provisions. And the following exchange occurred between him and Secretaries Dillon and Ball:

Senator AIKEN. * * *.

The Senator from Alabama asked what the relationship of OECD would be to GATT, and you said there would be no relationship whatsoever.

But reading this pledge to pursue efforts to reduce or abolish obstacles to the exchange of goods and services and current payments, makes one wonder whether OECD intends to operate parallel to GATT. What is the purpose there?

Secretary DILLON. Well, in the field of capital flow and money, the GATT does not operate, and in that field I think that OECD would operate.

We have always had a completely free regime for the flow of our capital and investments overseas; since the war, certainly, and probably for quite some time before that, the European countries have not.

Now that their currencies are becoming convertible, it is in our interest to press for a greater freedom of these capital flows so that European funds will come to the United States for investment with greater ease than is presently the case. This would be a forum through which this objective would be sought, and that is what I think is referred to here when they talk about current payments and liberalization of capital movements.

Senator AIKEN. But GATT and OECD would perform parallel functions as they relate to removal of trade barriers.

Secretary DILLON. Well, that is the specific policy of the GATT, and in OECD it is not its specific policy.

However, the countries agree that they will pursue their efforts individually, that is, to reduce and abolish obstacles.

Now, by obstacles to the exchange of goods, we do not mean tariffs.

What is really meant there are discriminatory provisions such as the chairman was talking about, which we have a few of in the agricultural field, and of which the European countries have many more.

This is a pledge to work toward reducing or abolishing these, but how quickly results will be achieved I do not know, and certainly this organization is not the primary forum in which this will be discussed.

Mr. BALL. Senator, I might add that this organization will not be an organization that makes trade rules or that enforces trade rules or that modifies existing trade rules.

There is a very clear distinction between what is contemplated here and the operations of the GATT in Geneva.

Senator AIKEN. It would simply make findings and, on the basis of those findings, make recommendations to its members or just release its findings?

Mr. BALL. The major interest of the United States in this, as Secretary Dillon has said, is in relation to the resolution of the existing problems between the Six and Seven. Our concern there is to see that in the consideration of this problem the interests of the United States are represented.

The chairman pursued this matter further and raised with the two executive branch witnesses some comments of the opposition to the OECD:

The CHAIRMAN. * * *.

Since I asked you my question about the opposition, I have sent for, and have received, this statement which is apparently the principal statement of the opposition to this treaty. I think it would be well for the record if you would comment on it.

First the ITO and OTC [Organization for Trade Cooperation] are described and how they were defeated by the Congress. Then the statement says "They both also sought to use the sanctity of an international agreement as a means of making permanently supreme the economic outlook of people then in the executive branch of the Government and especially in the State Department."

Do you think this is a true characterization of this agreement?

Secretary DILLON. Not at all, Mr. Chairman.

The other two agreements did provide a mechanism for establishing trade rules and, as such, they would have much more explicitly recognized the GATT.

The executive branch, at that time, felt that this was advisable because it was thought that the GATT was a useful instrument to prevent discrimination.

But the OECD has nothing whatsoever to do with trade rules at all. We have made that very clear. We would be glad to repeat it again. It does not reflect the philosophy of any particular group.

It is a broad, bipartisan measure that is in the national interest, and it simply recognizes the new facts of this era of convertibility, that we have to have a forum for the interchange of economic information, and where we can develop closer coordination and exchange views on methods and means by which each of our countries is successful in pursuing the objectives, its own objectives, of greater economic growth.

The CHAIRMAN. The statement says:

"While Congress has the constitutional authority and responsibility to regulate our foreign commerce, it could no longer do so without encountering and, perhaps running afoul, of provisions of the international agreement."

Do you think that is true?

Secretary DILLON. No, sir.

The CHAIRMAN. It says:

"Ratification of the agreement would, therefore, transfer some of the most meaningful aspects of the enumerated congressional powers into the hands of the Executive without bothering about a constitutional amendment. Surrender by Congress in this matter would mean breaking faith with the electorate and, in fact, betrayal of its trust."

Would you think it is a true statement?

Secretary DILLON. It would not transfer one single thing from the Congress to the Executive.

The CHAIRMAN. It states:

"How would this come about? It would come about through an authorization of membership in an international organization having aims which could not be carried out without entrenching upon the functions of Congress."

Mr. BALL. As has been pointed out repeatedly here, Mr. Chairman, the decisions of this organization can only be carried out through the constitutional processes of the United States. It does not add, it does not detract one bit from the powers of Congress. It does not expand the powers of the Executive.

Secretary DILLON. That was the very reason that that language was specifically written into the charter in subparagraph 3 of article 6, so that there could be no misunderstanding on this subject. We were afraid that otherwise some people would misinterpret this thing. But with that language in there there can be no misunderstanding.

The CHAIRMAN. So it is very clear that any specific agreement must return to the Congress and follow the usual procedure. None is authorized in advance by this agreement?

Secretary DILLON. That is correct.

Senator Sparkman suggested that a memorandum outlining the history of the GATT "from the standpoint of its consideration by Congress," along with some background on its activities, would be helpful to the committee. The Legislative Reference Service of the Library of Congress was asked to prepare such a memorandum. It appears on page 102 of the printed hearings.

Functions of DAC.—Senator Sparkman was interested in whether the DAC would be an operating agency, and, if so, would there be any overlapping of its functions with those of other multilateral organizations, such as the International Bank for Reconstruction and Development (IBRD).

His question produced the following exchange:

Mr. BALL. I would like to point out a distinction here which, I think, could be the subject of some confusion. This is not going to be an operating agency in the area of foreign assistance. The OECD will provide a forum in which the problem of foreign assistance can be freely discussed among the nations which have the resources to contribute to that effort.

Senator SPARKMAN. Is that true of the OECD and the DAC, both?

Mr. BALL. Yes. The DAC is simply a committee established under the OECD in which the problems of assistance are going to be discussed, and in which the effort will be made to mobilize the greatest amount of effort and resources for the purpose. But it is not contemplated that this will be an agency which administers aid.

Secretary DILLON. Senator, I might say that in the meetings that we had last year of this Development Assistance Group, which is the predecessor organization, the World Bank and some of the U.N. agencies participated as observers, and they worked very closely with this group.

This group might lead to closer coordination of national efforts, but, as Secretary Ball says, it has nothing to do with operations and therefore would not interfere with these other agencies at all.

Secretary Dillon added to the committee's understanding of the purpose and function of the DAC with this observation:

We found when we started to discuss this last year in the earlier meetings of the Development Assistance Group, which will be the predecessor of this committee, that there was not even agreement on the definition of what was foreign aid. Some countries were calling foreign aid ordinary exports, which they financed on a 2- or 3-year basis, and so there was a good deal of discussion on that. We are now discussing what is aid and what is simply ordinary exports that one is financing. Statistics are being gathered, and it will become clear whether one or more of the big industrialized countries is not doing what it is obviously supposed to be doing. For any country not carrying a fair share of the burden, there will be moral pressure on that country to do better.

Now, certainly no one could expect the United States to do any more since we have been carrying the bulk of the load from the beginning with help from particularly the French and the British.

So, therefore, the effect of this committee will be, from our point of view, since we are already doing what we should, to throw the spotlight on those who have not yet met their full responsibilities. In that way it is a very important financial tool and very helpful to the United States in seeing that the program is better shared.

Relationship to NATO.—The chairman asked whether the OECD might have the effect of downgrading the importance of NATO. The opinion of the executive branch witnesses is that the two organizations will perform complementary functions. Senator Morse pursued the matter further, and drew this comment from Secretary Dillon:

I would like to say one thing about this. One field in which the OECD will be active, which is the responsibility of the Development Assistance Committee, is the coordination and discussion of policy for development assistance to underdeveloped countries throughout the world, many of which are neutral countries.

This is a function which simply could not be carried out successfully by NATO, because NATO is looked upon as a military alliance, and a strong partisan of one side—our side—in the cold war.

So these neutral countries of Asia and Africa would not feel comfortable if their aid was being coordinated by that sort of an organization. They have made that very clear. So that is the great advantage of having the OECD, which does not have that connotation and which does have all the neutral countries of Europe as members.

Senator MORSE. Mr. Secretary, I could not agree with you more. That is why I pursue this matter a moment longer. Secretary Ball pointed out that Sweden and Switzerland will be members of OECD. They are not members of NATO.

Legal interpretation.—Several committee members were especially interested in having a precise understanding of articles 5 and 6. Specifically, they were concerned with what, if anything, distinguishes the "decisions" of 5(a) from the "recommendations" of 5(b); also whether article 6(3) clearly and adequately protects the balance between the legislative and executive branches of the Government. In response to a committee request, the Legal Adviser to the Department of State prepared a memorandum addressed to these specific questions. It appears as Appendix 4 to this report. Under article 5(a), the Organization may "take decisions which, except as otherwise provided, shall be binding on all the Members." The Legal Adviser says: "Thus, by the very terms of a decision, it may be restricted in its obligatory application to only certain of the members of the Organization."

Under 5(b), the Organization may "make recommendations to Members * * *". The Legal Adviser says:

* * * Recommendations may recommend a course of action by members, or study of a matter, or adherence to an international agreement drafted in an OECD committee, etc. For example, the OECD will normally deal with substantive problems such as economic policy and assistance to the less-developed countries by exchanging information and by informal discussions. To the extent that additional action were necessary, this would normally be taken by the OECD Council in the form of a recommendation to member governments. Thus, the OECD Council might follow a discussion of assistance to the less-developed countries by a recommendation to member governments that they increase the length of the credits extended to the less-developed countries. In such cases, the member governments would not be legally bound by the recommendations, but they would endeavor to carry out the recommendations.

The Legal Adviser says that articles 1 and 2 are—

void of any grant of power to the Executive, and the power, in any particular case, of the U.S. Executive to bind the United States must be sought and found in an independent source outside the [OECD] Convention.

His conclusion is that—

paragraph 3 of article 6 allows for full compliance with U.S. constitutional procedure and the division of functions between the Executive and the Congress.

Other questions.—Senator Aiken asked about the anticipated size of the OECD staff and the cost of maintaining the Organization. The following exchange occurred between him and Secretary Dillon:

Senator AIKEN. Mr. Secretary, how large an organization do you expect this to be in terms of personnel?

Secretary DILLON. We have a feeling that this will be smaller than the present OEEC organization because this organization had a very considerable number of personnel engaged in certain functions which would probably not be continued. I think that the total effort in Paris will be several hundred.

The figures, I think, on the OEEC now are somewhere under 1,000 people working in that organization.

Senator AIKEN. It may be 1,000. What was the estimated cost of maintaining the organizaton a year?

Secretary DILLON. Well, the OEEC's costs were approximately $4 million, so we thought that our share would be about $1 million, if we had the same assessment as our assessment in NATO, which is roughly 25 percent.

Senator AIKEN. 25 percent.

Secretary DILLON. We might have a smaller assessment here because this is a larger organization somewhat. In NATO our assessment is 24.2 percent. Here there are the few extra smaller countries, so it might be possible that we could negotiate something between 20 and 25 percent, which, I think, would be fair.

Senator Morse asked whether consideration was given to inviting Japan to be a full-fledged member of the OECD. Secretary Dillon replied that the United States "would like to see that happen." However, the European countries, while agreeing to Japanese participation in the DAC, opposed a general membership for Japan. Secretary Dillon observed that this feeling might change and at some later date Japan could be invited into full OECD membership.

The chairman and Senator Morse indicated that their further questions would be submitted in written form. The contents of their correspondence can be found in the appendix to the record of the OECD hearings. Among other things, their questions dealt with the balance of payments problem; discriminations against U.S. products; restrictions against capital movements in and out of the OECD countries; the U.S. tariff position and the benefit to the United States of GATT participation; examples of decisions that might be made by the OECD Council in regard to the aims set forth in article 1.

Among those who asked to bring their views on the OECD before the committee were three Members of Congress, Senator Jacob K. Javits of New York; Representative W. J. Bryan Dorn of South Carolina; and Representative James C. Davis of Georgia. Senator Javits supports the convention. Congressmen Dorn and Davis oppose it on the grounds that it could, in their view, expand the authority of the executive branch to regulate foreign commerce. They were followed by seven public witnesses, six of whom oppose the convention for reasons similar to those expressed by Congressmen Dorn and Davis. The committee received over 600 communications concerning the OECD. There was an approximately even division between those who were for, and those who were against the convention.

Further committee action.—On March 1, the committee met in executive session to hear further testimony from Secretaries Dillon and Ball. Senator Long questioned the language of article 2(d), and the following explanation was offered by Secretary Dillon:

What this means—the English text was construed by the people who drafted the language, and by those who signed it, to mean that they would pursue their efforts to reduce or abolish obstacles and to maintain and extend the liberalization of capital movements.

In other words, the "maintain and extend the liberalisation of capital movements" follows after "pursue their efforts to," and therefore the agreement is to pursue efforts to maintain and extend the liberalization of capital movements. No flat commitment is made to maintain and extend them; in the French text, which is equally valid, that is made very clear, because the word "to" is in there in the French text.

There is a word "to" before "maintain."

* * * * * * *

The question arose again when Senator Gore asked this question of Secretary Ball and the Legal Adviser to the Department of State, Mr. Chayes:

If by this treaty we specifically agree to maintain and extend the liberalization of capital movements, would a statutory enactment contrary to such liberalization of capital movement be in conflict with the treaty?

Mr. Chayes responded and the following exchange ensued:

Mr. CHAYES. Well, Senator, your hypothetical case depends upon reading article 2(d) as an absolute engagement to maintain and extend the liberalization of capital movements.

I think the Secretary has already said that the article is to be construed as an engagement merely to pursue efforts to maintain and extend the liberalization of capital movement.

Senator GORE. May I ask a question right there? Suppose that instead of the Secretary's interpretation, the Court should hold that, in fact, this is an agreement to maintain and extend the liberalization of capital movements; what would then be the confrontation?

Mr. CHAYES. Well, with deference, Senator, I cannot conceive a court so holding in view of the fact that the French and English text have equal status, and any ambiguity that appears in the English text is fully clarified by the French text.

Senator Gore was specifically concerned with the meaning of the term "current payments" and the phrase "liberalisation of capital movements" as they appear in article 2(d). The Department of the Treasury, in order to define these terms precisely, offered a memorandum that appears in the appendix of the printed hearings.

Several members sought further assurance that none of the provisions of the convention could endow the President with authority that he does not already have; these members also sought further clarification of the constitutional guarantees contained in article 6(3). The Legal Adviser, Mr. Chayes, responded with a memorandum dated March 6, which appears in appendix 5 to this report.

The committee met again in executive session on March 6. Under Secretary Ball and the Legal Adviser, Mr. Chayes, were present. Some members were interested in U.S. policies regarding most-favored-nation treatment. Upon request, the Department of State submitted one memorandum explaining American policy on this subject, and another which set forth provisions of the GATT that allow contracting parties to adopt discriminatory policies under certain circumstances. These memorandums may be found on page 245 of the hearings.

Senator Williams observed that the President's authority under the Trade Agreements Act is discretionary. He asked whether a decision by the OECD Council might compel the President to act within the scope of his authority, thus depriving him of his option not to act. This produced the following exchange between the Senator, Under Secretary Ball, and Mr. Chayes:

Mr. BALL. No; he could not bind himself to do anything unless he has the power to do. I do not quite understand how this could possibly occur—do you, Mr. Chayes?

Mr. CHAYES. Well, I do not think he could even bind himself to waive his discretion in the case of a subsequent escape clause proceeding since he does not have, I do not think, constitutional power to waive that subsequent discretion.

Mr. BALL. You see, he has to make a finding.

Senator WILLIAMS. That is right.

Mr. BALL. We cannot waive his power to make the finding. He has to make the finding to comply with the statute. Otherwise he has no power.

* * * * * * *

Mr. CHAYES. I do not know just what the terms of our arrangements in GATT are. But it is perfectly clear that in the case of any agreement in GATT, or any other agreement under the Trade Agreements Act—and notice when we are talking about the hypothetical case of an agreement under this Convention, it is only an agreement carried out within the terms of the authority delegated by the Trade Agreements Act—no such agreement can be made until the President's discretion has been exercised in accordance with all the terms and conditions of the act.

Senator Hickenlooper asked whether any provision of the convention could give the President tariff-making authority and prevent the Congress from taking back that authority.

Under Secretary Ball and Mr. Chayes replied that this would not be possible.

The committee feels that in giving its advice and consent the Senate must emphasize, as an inherent part thereof, that it accepts and relies upon the assurances of the executive branch of the Government that nothing in the Convention enlarges, diminishes, or alters the powers of the President or the Congress in respect to any substantive actions taken or that may be taken by the Organization for Economic Cooperation and Development and that a clear expression of such interpretation and understanding should be incorporated as an integral part of such advice and consent. The committee felt that the resolution of ratification should contain the relevant assurances that had been offered by Secretary of State Herter, Secretary of the Treasury Dillon, Under Secretary Ball, and the Legal Adviser of the Department of State. Secretary Herter's statement appears in his letter of January 16 to President Eisenhower, which can be found on page 2 of the message from the President transmitting the convention to the Senate (Ex. E, 87th Cong., 1st Sess.). Statements of the other deponents may be found in this report and appendixes thereto. The full text of the resolution of ratification itself follows:

RESOLUTION OF RATIFICATION

Having regard to and in reliance on the statement in the letter of January 16, 1961, from Secretary of State Herter to President Eisenhower and transmitted by him to the Senate on January 17, 1961, that "the U.S. representative will not have any additional powers in substantive matters to bind the United States after the convention enters into force than now exist in the Executive, but that any act of the Organization outside the power of the Executive will require action by Congress or the Senate, as the case may be, before the United States can be bound," and having regard to and in reliance on the testimony of Secretary of the Treasury Dillon and Under Secretary of State Ball in behalf of the administration, and having regard to and in reliance on the Opinion of the Legal Adviser of the Department of State dated March 6, 1961, and quoted in the committee report on this convention:

Resolved (*Two-thirds of the Senators present concurring therein*), That the Senate advise and consent to the ratification of the Convention on the Organization for Economic Cooperation and Development, together with two protocols relating thereto, signed at Paris on December 14, 1960, by representatives of the United States of America, Canada, and the 18 member countries of the Organization for European Economic Cooperation (Executive E, 87th Congress, 1st session), with the interpretation and explanation of the intent of the Senate that nothing in the convention, or the advice and consent of the Senate to the ratification thereof, confers any power on the Executive to bind the United States in substantive matters beyond what the Executive now has, or to bind the United States without compliance with applicable procedures imposed by domestic law, or confers any power on the Congress to take action in fields previously beyond the authority of Congress, or limits Congress in the exercise of any power it now has.

CONCLUSION

The Committee on Foreign Relations believes that the OECD member countries are undergoing the gravest test of their collective history. To prevail will depend, as much as anything else, on their ability to promote stability and growth within their delicately balanced, interdependent economies. Yet even this will not be enough, if the product of this growth is not in sufficient measure devoted to programs that will encourage the development of less favored peoples in a way that is consonant with their best purposes. If the energies and resources of the aspirant and newly independent peoples were turned to uncongenial purposes, the consequences for Western civilization would ultimately be decisive.

This thesis is understood by the leaders of both the Soviet Union and the United States, and apparently by a majority of the people of the United States. It is also understood by some, but by no means all, of the leaders of West Europe. Many of them do not yet understand either the moral imperatives or the cold logic of foreign assistance. And what is true of these leaders can be safely said to apply, as well, to their constituents.

In that light, the OECD will be an educational forum. Terms can be defined. Foreign aid itself is a term that badly needs definition. To some, exports financed with short term, high interest credits, are foreign aid, and sums for this purpose are cited, not as investment, but as evidence of good faith. To others, funds invested in a colony fall within the definition of foreign aid. The American experience with foreign aid must be brought to bear upon the consciousness of other capital exporting countries. Bilateral talks, even if conducted at the White House level, are no substitute for the education that can be spread throughout the OECD membership by joint exposure to the same information, to the philosophy and the logic that have motivated American foreign aid from the beginning.

If Europeans have not developed a keen appreciation for foreign aid, it is also true that Americans have been laggard in acknowledging the economic interdependence of the Atlantic Basin countries. The truth is that the West can no longer tolerate economic disequilibrium. Too much depends on the vigor of its interdependent economy, greater by far than the sum of the individual parts.

More important than the collective GNP ($775.5 billion) of the OECD members are the scientific and technical resources upon which it is built. With the OECD, these resources can be mobilized and directed toward productive purposes. For the first time, a group of countries with common interests, beset by common problems, will be free to discuss their goals and problems within an organization designed for precisely that purpose.

This is a time of sweeping political, social, and technological change. History is being shaped within a swirl of events that often develop with bewildering speed. The committee believes that the OECD will enable its members to see these events in a broader and, hence, more relevant perspective. It will enable them to look above the crises of today to problems that lie ahead; to dispose of many problems in a systematic, orderly fashion, thus avoiding the harsh urgency that so often distorts bilateral efforts to solve problems that become critical overnight. The committee, therefore (by a vote of 16 to 0), recommends that the Senate give its advice and consent to the ratification of the pending treaty.

APPENDIXES

Appendix 1

MEMORANDUM OF UNDERSTANDING ON THE APPLICATION OF ARTICLE 15 OF THE CONVENTION ON THE ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

Article 15 of the Convention on the Organisation for Economic Co-operation and Development (hereinafter called the "Convention") provides that decisions, recommendations and resolutions (hereinafter called "acts") of the Organisation for European Economic Co-operation shall require approval of the Council of the Organisation for Economic Co-operation and Development (hereinafter called the "Council") to be effective after the coming into force of the Convention.

Pursuant to a Resolution adopted at the Ministerial Meeting of 22nd–23rd July, 1960, a Preparatory Committee has been established and instructed to carry further the review of the acts of the Organisation for European Economic Co-operation, to determine which acts should be recommended to the Council for approval, and to recommend, where necessary, the modifications required in order to adjust these acts to the functions of the Organisation for Economic Co-operation and Development.

At the said Ministerial Meeting it was agreed that there should be the maximum possible degree of certainty as regards approval by the Council of acts of the Organisation for European Economic Co-operation in accordance with the recommendations of the Preparatory Committee; it was also agreed that Canada and the United States, not being Members of the Organisation for European Economic Co-operation, should have a certain latitude with respect to the said recommendations.

Therefore the Signatories of the Convention have agreed as follows:

1. The representatives of the Signatories on the Council shall vote for approval of acts of the Organisation for European Economic Co-operation in accordance with the recommendations of the Preparatory Committee, except as otherwise provided hereinafter.

2. Any Signatory which has not been a Member of the Organisation for European Economic Co-operation shall be released from the commitment set out in paragraph 1 with respect to any recommendation or part thereof of the Preparatory Committee which it specifies in a notice to the Preparatory Committee no later than ten days after the deposit of its instrument of ratification or acceptance of the Convention.

3. If any Signatory gives notice pursuant to paragraph 2, any other Signatory, if in its view such notice changes the situation in regard to the recommendation or part thereof in question in an important respect, shall have the right to request, within fourteen days of such notice, that the Preparatory Committee reconsider such recommendation or part thereof.

4. (*a*) If a Signatory gives notice pursuant to paragraph 2 and no request is made pursuant to paragraph 3, or, if such a request having been made, the reconsideration by the Preparatory Committee does not result in any modification of the recommendation or part thereof in question, the representative on the Council of the Signatory which has given notice shall abstain from voting on the act or part thereof to which the recommendation or part thereof in question pertains.

(*b*) If the reconsideration by the Preparatory Committee provided for in paragraph 3 results in a modified recommendation or part thereof, the representative on the Council of the Signatory which has given notice may abstain from voting on the act or part thereof to which the modified recommendation or part thereof pertains.

(*c*) Abstention by a Signatory pursuant to sub-paragraph (*a*) or (*b*) of this paragraph with respect to any act or part thereof shall not invalidate the approval of that act or part which shall be applicable to the other Signatories but not to the abstaining Signatory.

5. The provisions of this Memorandum relating to actions to be taken before the voting in the Council shall come into force upon its signature; the provisions relating to the voting in the Council shall come into force for each Signatory upon the coming into force of the Convention as regards that Signatory.

In witness whereof, the undersigned have appended their signatures to this Memorandum.

Done in Paris, this fourteenth day of December, Nineteen Hundred and Sixty, in the English and French languages, both texts being equally authentic, in a single copy which shall be deposited with the Government of the French Republic, by whom certified copies will be communicated to all the Signatories.

[Signatures omitted.]

APPENDIX 2

Official assistance to the less-developed countries by OECD countries and Japan

[Dollars in millions]

	1956	1957	1958	1959	1956–59
Austria:					
GNP	$4,238	$4,665	$4,938	$5,264	$19,105
Aid	$2	$1	$6	$4	$13
Aid as percent of GNP	0.05	0.02	0.12	0.08	0.07
Belgium-Luxembourg:					
GNP	$10,860	$11,650	$11,616	$12,000	$46,126
Aid	$17	$24	$23	$52	$116
Aid as percent of GNP	0.16	0.21	0.20	0.43	0.25
Denmark:					
GNP	$4,461	$4,769	$4,918	$5,270	$19,418
Aid	$3	$1	$4	$5	$13
Aid as percent of GNP	0.07	0.02	0.08	0.09	0.07
France:					
GNP	$37,513	$41,867	$47,532	$51,000	$177,912
Aid	$487	$639	$787	$954	$2,867
Aid as percent of GNP	1.30	1.53	1.66	1.87	1.61
Germany:					
GNP	$46,048	$49,905	$52,929	$56,645	$205,527
Aid	$21	$46	$78	$107	$253
Aid as percent of GNP	0.05	0.09	0.15	0.19	0.12
Ireland:					
GNP	$1,510	$1,588	$1,630	$1,710	$6,438
Aid		$1	$1	$1	$2
Aid as percent of GNP		0.06	0.06	0.06	0.03
Italy:					
GNP	$23,414	$25,088	$26,638	$27,970	$103,110
Aid	$16	$16	$31	$17	$81
Aid as percent of GNP	0.07	0.06	0.12	0.06	0.08
Netherlands:					
GNP	$8,610	$9,315	$9,592	$10,175	$37,692
Aid	$33	$34	$41	$43	$151
Aid as percent of GNP	0.38	0.37	0.43	0.42	0.40
Norway:					
GNP	$3,725	$3,950	$3,894	$4,100	$15,669
Aid	$1	$2	$3	$4	$10
Aid as percent of GNP	0.03	0.05	0.08	0.10	0.06
Portugal:					
GNP	$1,945	$2,015	$2,071	$2,135	$8,166
Aid	$7	$5	$4	$21	$38
Aid as percent of GNP	0.36	0.25	0.19	0.98	0.47
Sweden:					
GNP	$9,470	$10,245	$10,623	$10,850	$41,188
Aid	$3	$12	$4	$10	$29
Aid as percent of GNP	0.03	0.12	0.04	0.09	0.07
Switzerland:					
GNP	$6,846	$7,355	$7,593	$8,000	$29,794
Aid	$1	$1	$3	$1	$5
Aid as percent of GNP	0.01	0.01	0.04	0.01	0.02
United Kingdom:					
GNP	$57,960	$61,328	$63,484	$65,700	$248,472
Aid	$208	$243	$264	$356	$1,070
Aid as percent of GNP	0.36	0.40	0.42	0.54	0.43
Total, above countries:					
GNP	$216,600	$233,740	$247,458	$260,819	$958,617
Aid	$799	$1,025	$1,247	$1,575	$4,648
Aid as percent of GNP	0.37	0.44	0.50	0.60	0.48
United States:					
GNP	$419,200	$442,500	$441,700	$478,000	$1,781,400
Aid	$2,144	$2,343	$2,415	$2,438	$9,340
Aid as percent of GNP	0.51	0.53	0.55	0.51	0.52
Canada:					
GNP	$30,182	$31,773	$32,509	$34,700	$129,614
Aid	$28	$46	$88	$57	$219
Aid as percent of GNP	0.09	0.14	0.27	0.16	0.17
Japan:					
GNP	$24,650	$28,050	$27,750	$30,000	$110,450
Aid	$16	$15	$205	$41	$277
Aid as percent of GNP	0.06	0.05	0.74	0.14	0.25

NOTES

1. GNP figures are at current market prices. The figures for 1959 are estimated.
2. Both the GNP and aid figures have been converted to dollars at current exchange rates.
3. Aid figures are based primarily on actual expenditures. For all the countries they include: (*a*) net official grants, (*b*) gross official bilateral loans of 5 years or over, (*c*) official contributions and subscriptions to international organizations paid during the period (i.e., net IBRD subscriptions, IFC capital contributions, contributions to the EEC Development Fund, net contributions to United Nations technical assistance and relief agencies). For the United States, the increase in U.S. holdings of local currencies derived from Public Law 480, title I sales is included to reflect the transfer of resources. For Japan, the yearly breakdown on gross official bilateral loans of 5 years or over is estimated. Reparations payments have not been included.
4. This definition of assistance has not been accepted by the countries involved and has no international standing.

APPENDIX 3

TABLE A.—*Importance of OECD countries as a market for less developed countries—Exports from less developed countries to OECD members by principal commodities, total exports, and proportion taken by OECD countries, 1959*

	Rubber	Tea	Cocoa	Coffee	Rice	Tobacco	Petroleum	Cotton [1]	Tin	Copper	All LDC exports
Imports from LDC's into—	*Thousand long tons*	*Metric tons*	*Thousand long tons*	*Thousand metric tons*	*Thousand metric tons*	*Thousand metric tons*	*Million metric tons*	*Thousand bales*	*Metric tons*	*Thousand metric tons*	*Millions*
Austria	11.3	534	10.0	9.8	1.6	1.9	0	48.6	0	2.6	$70
Belgium/Luxembourg	14.3	60	10.0	54.8	22.5	11.2	6.7	269.5	2,001	180.3	580
Canada	45.3	16,739	12.5	56.8	8.2	.3	15.8	201.3	967	0	440
Denmark	6.2	843	3.4	38.4	0	6.0	(2)	25.4	0	.5	80
France	120.4	1,496	55.3	197.0	82.4	12.2	28.8	686.2	339	53.8	1,880
Germany	143.9	6,965	102.3	136.7	45.4	18.3	16.5	889.9	50	219.3	1,710
Greece	1.9	109	2.4	7.2	1.3	0	1.3	1.1	88	.2	60
Iceland	----	----	----	1.6	0	0	0	0	0	0	(2)
Ireland	3.8	9,962	5.8	.4	0	.1	.9	13.9	0	0	80
Italy	56.1	1,315	26.2	83.6	.6	0	22.5	323.1	2,342	76.7	860
Netherlands	20.6	9,605	74.3	50.3	39.9	12.9	12.4	288.9	80	10.7	750
Norway	2.9	71	4.0	25.1	.5	.7	.1	12.0	0	0	120
Portugal	4.8	167	1.0	10.5	.7	.8	1.2	222.4	0	2.8	120
Spain	21.4	57	21.4	.1	0	(3)	7.2	137.4	0	14.1	(3)
Sweden	21.3	1,040	6.7	68.0	0	.6	2.4	31.5	0	30.7	300
Switzerland	6.4	(3)	12.0	(3)	(3)	(3)	(3)	120.0	57	14.2	140
Turkey	3.8	5,912	.8	1.0	0	0	0	0	163	0	(2)
United Kingdom	167.3	228,272	77.2	52.9	23.2	57.6	46.2	777.2	0	336.2	3,920
United States	557.4	45,258	204.7	1,396.6	0	14.5	58.7	136.3	24,162	206.4	6,040
Total OECD imports from LDC's	1,209.0	328,402	630.0	2.240.9	226.1	137.0	220.9	4,184.7	30,249	1,148.6	17,150
Total world imports from LDC's	2,042.5	479,655	750.4	2,511.8	3,833.7	241.7	317.3	8,115.0	50,052	1,430.0	26.210
OECD imports as percentage of world imports from LDC's	59	68	84	89	6	57	70	52	60	80	65

[1] Cotton figures are for crop year 1958–59.
[2] Negative.
[3] Not available.

TABLE B.—*Proportion of export earnings of selected less developed countries derived from principal primary products, 1959*

[Percentages]

Countries	Cocoa	Coffee	Copper	Cotton	Petroleum	Rice	Rubber	Tea	Tin	Tobacco
Bolivia									69	
Brazil	5	57		2						
Chile			69							
Colombia		77			16					
Costa Rica	5	50								8
Dominican Republic	17	13								
Ecuador	13	3								
El Salvador		64		21						
Guatemala		71								
Haiti		55								
Honduras		24								
Mexico		9	4	26						
Nicaragua		21		45						
Panama	3									
Paraguay				7						
Peru			8	22	5					
Venezuela					87					
Egypt				71		1				
Iraq					93					
Sudan				60						
Syria				48						
Ethiopia		61								
Ghana	67									
Burma				2		71				
Ceylon							17	60		
India								20		
Indonesia					26		48		4	
Malaya							66		10	
Pakistan				12						
Thailand						34	31		6	
Vietnam						32	63			

APPENDIX 4

DEPARTMENT OF STATE,
February 27, 1961

Hon. J. W. FULBRIGHT,
Chairman, Committee on Foreign Relations,
U.S. Senate.

DEAR MR. CHAIRMAN: In the course of the hearings on the Convention on the Organization for Economic Cooperation and Development on Wednesday, February 15, 1961, before the Foreign Relations Committee a request was made for a memorandum setting forth the legal analysis of article 5 and article 6.

I attach such a memorandum and hope it will be helpful to your committee in the consideration of the convention. I wish to point out that the Department of Justice has been consulted in the preparation of this memorandum.

Sincerely yours,

ABRAM CHAYES, *The Legal Adviser.*

Enclosure: Memorandum.

MEMORANDUM

Article 5 of the Convention on the Organization of Economic Cooperation and Development reads as follows:

"In order to achieve its aims, the Organization may:

"(a) take decisions which, except as otherwise provided, shall be binding on all the Members;

"(b) make recommendations to Members; and

"(c) enter into agreements with Members, non-member States and international organizations.

Article 6 reads as follows:

"1. Unless the Organization otherwise agrees unanimously for special cases, decisions shall be taken and recommendations shall be made by mutual agreement of all the Members.

"2. Each Member shall have one vote. If a Member abstains from voting on a decision or recommendation, such abstention shall not invalidate the decision or recommendation, which shall be applicable to the other Members but not to the abstaining Member.

"3. No decision shall be binding on any Member until it has complied with the requirements of its own constitutional procedures. The other Members may agree that such a decision shall apply provisionally to them."

It appears that the discussion in the committee which gave rise to the request for the present memorandum concerned in the main article 5 and article 6, paragraph 3.

Under article 5(a) the Organization may act by taking decisions. Such decisions are binding on all the members, except as otherwise provided. Thus, by the very terms of a decision, it may be restricted in its obligatory application to only certain of the members of the Organization.

Under article 5(b) the Organization may act by making recommendations. As the term signifies, these are not of an obligatory nature, but a member would be expected to endeavor to carry out such a recommendation, unless the member abstained from voting for it. Recommendations may recommend a course of action by members, or study of a matter, or adherence to an international agreement drafted in an OECD committee, etc. For example, the OECD will normally deal with substantive problems such as economic policy and assistance to the less-developed countries by exchanging information and by informal discussions. To the extent that additional action were necessary, this would normally be taken by the OECD Council in the form of a recommendation to member governments. Thus, the OECD Council might follow a discussion of assistance to the less-developed countries by a recommendation to member governments that they increase the length of the credits extended to the less-developed countries. In such cases, the member governments would not be legally bound by the recommendations, but they would endeavor to carry out the recommendations.

Under article 5(c) the Organization may enter into agreements with members, nonmembers, or international organizations. One such type of agreement is referred to in Supplementary Protocol No. 2, namely, an agreement by the Organization with Canada or a nonmember government regarding the legal capacity and privileges and immunities of the Organization on the territory of Canada or such nonmember government. Also the Organization might enter into an agreement with another international organization, such as the International Monetary Fund, for participation of representatives of the IMF as observers in certain committees of the OECD.

The question was raised in the hearings before the committee whether the statement of the aims of the Organization in article 1 and the agreement in elaboration of such aims in article 2 could be construed, assuming Senate ratification, to confer power upon the executive branch of the United States Government acting through its representative on the Council of the Organization, to bind the United States by participating in a decision of the Organization within the fields described in articles 1 and 2 which define the substantive scope of the Organization. As stated in the letter of January 16, 1961 of the Secretary of State to the President, which the President enclosed with his message to the Senate of January 17, 1961, and as reiterated by Government spokesmen at the hearings, it is not considered that by the convention the Executive will have any additional powers in substantive matters that now exist in the Executive. In short, articles 1 and 2 set forth the general agreement between the member nations and limit the proper scope of activities of the Organization; these articles are void of any grant of power to the Executive, and the power, in any particular case, of the United States Executive to bind the United States must be sought and found in an independent source outside the convention.

With this as background, consideration may now be given to article 6, paragraph 3. This important paragraph states that no decision shall be binding on a member until it has complied with the requirements of its own constitutional procedures.

Thus, if a decision were proposed to the Council for the establishment of a committee of representatives of member governments to study the promotion of tourism, the executive branch would consider it had power to agree to such a decision. Similarly, if a decision were proposed to the Council for the establishment of a fund for the period of a year, contributed to by all members, to encourage tourism in member countries, the United States Executive would consider it had power to agree to such a decision, if the United States Congress had authorized and appropriated funds for the promotion of tourism to the United States. If no such congressional authorization and appropriation existed, the executive branch through its representative would either veto the decision, or abstain (thus permitting the decision to become binding as to other member countries) or approve, subject to compliance with United States constitutional procedures. In this last event, appropriate United States congressional action would have to be taken before the decision could be binding on the United States. Similarly, a decision might be proposed to the Council involving an international agreement of a type which would require Senate advice and consent under United States treaty procedure. In this case, again, the United States representative could veto, abstain, or approve subject to compliance with United States constitutional procedures. In this last event, Senate advice and consent would need to be given before the decision could be binding on the United States. In conclusion, it is our view that paragraph 3 of article 6 allows for full compliance with United States constitutional procedures and the division of functions between the Executive and the Congress.

It may be noted that it is expected that most of the decisions taken by the OECD Council which will be binding on member governments will not pertain to substantive matters but will pertain to administrative matters, such as the establishment of committees and working parties. For example, the OECD Council will have to take decisions to establish the appropriate subsidiary bodies of the OECD. Council decisions will also be taken concerning the terms of reference of these committees. Later Council decisions will be taken covering the activities of these committees.

Appendix 5

March 6, 1961.

OPINION OF THE LEGAL ADVISER

The Legal Adviser of the State Department is of the opinion that nothing in the Convention on the Organization for Economic Cooperation and Development confers any power on the Executive to bind the United States in substantive matters beyond what the Executive now has, or on the Congress to take action in fields previously beyond the authority of Congress. Conversely, nothing in the convention diminishes the power of the Executive or Congress in these respects.

The attached memorandum sets forth the reasoning underlying this opinion.

Abram Chayes, *The Legal Adviser.*

Memorandum

1. There is nothing in the convention which expands or enlarges the power of the Executive in substantive matters.

Article 1 states the aims of the Organization and article 2 sets forth the general agreement of the members in elaboration of these aims. Then article 5 states that the Organization may take decisions and article 6 describes the process by which these decisions be taken. This process provides two safeguards for the United States. In the first place no decision may be imposed on it without its consent. Secondly, that consent must be given in compliance with the requirements of U.S. constitutional procedures before the decision becomes binding upon us.

The argument has been intimated that since the Organization under article 5 is authorized to take decisions and since the executive branch will be representing the United States in the Organization, the convention will operate to give the Executive power to agree on decisions in the substantive fields covered by articles 1 and 2. This argument is based on the erroneous assumption that the convention in any way concerns itself with the distribution of powers within the United States or any other member state. Properly viewed, articles 1 and 2 merely set forth a general agreement between the member nations on broad lines of public policy and define the area of concern of the Organization. Under article 5 the Organization may take decisions, but the convention is silent as to the process by which a member nation, within its own internal system, arrives at the point where it may cast an effective vote in favor of a particular decision. Articles 1 and 2 are void of any grant of power to the Executive. Thus, the power of the United States to cast a favorable vote and bind the United States in any particular case must be sought in a source outside the convention.

Paragraph 3 of article 6 was urged upon the other countries by the United States. The United States in the negotiations emphasized that under our constitutional system certain matters were in the purview of Congress and that the agreement of the United States to Council decisions on such matters even after the ratification of the convention would remain subject to further action by the Congress before being binding on the United States. Paragraph 3 of article 6 would have been unnecessary and meaningless if the mere ratification of the convention served to clothe the Executive with powers to take action in the fields covered by articles 1 and 2.

It may be pointed out that the view that the convention does not enlarge the power of the Executive in substantive matters (1) was stated in the letter of January 16, 1961, of Secretary of State Herter to President Eisenhower which he enclosed with his message to the Senate of January 17, 1961, (2) was repeated several times by Secretary Dillon and Under Secretary Ball at the hearings before the Foreign Relations Committee, and (3) was developed in some detail in a memorandum of the Legal Adviser of the State Department concurred in by the Department of Justice and enclosed with a letter of February 27, 1961, from the Legal Adviser to the chairman of the Foreign Relations Committee.

2. There is nothing in the convention which expands or enlarges the power of the Congress to take action in fields previously beyond the authority of the Congress.

The argument appears to have been made that the provisions of articles 1 and 2 may in some way serve as the source of authority for Congress to legislate in the future in fields which are reserved to the States by the 10th Amendment. As was stated at the hearings by Government spokesmen, articles 1 and 2 define the broad aims and goals of the Organization. The language of article 2 is that of agreeing to "promote," "pursue policies," "pursue * * * efforts" and "contribute * * * by appropriate means." The concrete steps by which the broad aims and goals are to be effectuated remains in the complete discretion of each member nation. We wish to emphasize the point made in Under Secretary Ball's letter to the chairman of February 27, 1961, that such language in article 2 does not constitute a commitment to take any concrete action or refrain from any concrete action. We are merely bound to consult and exchange views and information in a regular and systematic manner on matters within the purview of the article. In our view this language cannot serve as any authorization to Congress to take any action it otherwise could not take.

In this connection it should also be pointed out that treaties, like laws, are subordinate to the Constitution. They cannot violate the Constitution.

Finally, reference is again made to paragraph 3 of article 6. This paragraph, on its face, defers to our constitutional system not only in its distribution of powers between the Executive and the Congress, but also in its distribution of powers between the Federal Government and the States.

3. Nothing in the convention diminishes the power of the Executive or Congress.

In the course of the hearings the question was raised whether provisions of article 2 might not override congressional actions or inhibit congressional actions on particular subjects. As stated before, the terms used in article 2 do not constitute commitments to take any concrete action or refrain from any concrete action. In this view, it is difficult to envisage any statute of Congress or any act of the Executive that could be inconsistent with the terms of article 2. We therefore conclude that the terms of article 2 will not diminish the powers of Congress or the Executive in the fields therein described.

O

Mr. Chairman:

Almost a year ago, in the earlier part of 1960, the Federal Reserve System began to lean against the incipient down-wind of what has come increasingly to be classified as the fourth cyclical decline of the postwar era.

Already, as the winter faded, and with it the inflationary psychology that had characterized the economic situation carrying over from 1959, bank reserve positions--which govern the ability of the banking system to expand loans--had been made less dependent on borrowed funds.

Then, with the spring in progress, the Federal Reserve moved further: first, to promote still greater ease in bank reserve positions; and next, beginning in May, to provide additional reserves to induce a moderate expansion in bank credit and the money supply.

In this period in particular, new supplies of reserve funds were injected into the economy by means of open market operations. The first effect was to enable member banks to reduce appreciably their reliance on borrowed reserves. After this was accomplished the added reserves went to support the potential for bank credit expansion. In these open market operations, from late March through July, the Federal Reserve paid out about $1.3 billion, net, for the Government securities it was buying on an increasing scale. After cushioning the reserve impact of a $500 million increase of currency in circulation and gold outflow, this sum made possible a $300 million reduction in member bank borrowing and a $500 million increase in member bank reserves.

But other means available for the execution of System policy were used as well, particularly after mid-1960.

In early June, and again in August, discount rates were reduced, by 1/2 percentage point each time. These reductions lowered the cost of member bank borrowings from the Federal Reserve Banks to 3 per cent from the 4 per cent level that had prevailed before.

In August also, and again in November, by actions taken in implementation of a 1959 Act of Congress, nearly $2 billion previously tied up in vault cash of member banks was released to assure ample coverage of heavy borrowing needs for the fall and pre-Christmas seasons. An additional $700 million was provided by further net purchases of U. S. Government securities.

After midyear, the task of monetary policy ~~had to cope with~~ was complicated by an outflow of gold exceeding $1.5 billion. Thus, a substantial part of the reserve funds provided by the System in this part of the year went to offset the effect of this outflow on member bank reserves.

Taking the year 1960 as a whole, the change in bank reserve positions was dramatic. From net borrowings from the Federal Reserve of $425 million in December 1959, member banks as a whole moved by December 1960 to a surplus reserve of $650 million. The total turn-around exceeded a billion dollars.

Nevertheless, the money supply showed a stubborn downtrend until mid-1960. In the spring, bank credit seemed to respond less promptly to easier reserve conditions than in comparable periods in the past. After May, however, the seasonally adjusted money supply did begin to reflect our actions. In the second half of the year, the money supply rose at an annual rate of about 1.5 per cent. By year end, it had risen to $140.5 billion, just below the end-of-1959 peak. The money supply has expanded further in January and February of this year. Indeed, the annual rate of increase calculated from the performance of these two months was in the neighborhood of 4 per cent and the total money supply is now above year-ago levels.

The savings and time deposits of banks continued to grow in 1960 and after midyear the pace of growth was unusually rapid. This increase in time deposits permitted an increase of total bank loans and investments for the year as a whole by $8.4 billion. That was twice as much as the year before.

Total credit in the economy in 1960 expanded by some $37 billion. That figure was about two-fifths less than the record expansion of $61.5 billion in 1959, on which I reported to you a year ago, and more nearly in line with total credit extensions of other recent years. The smaller growth in 1960 was attributable to reduced pressure of borrowing demand, especially on the part of the Federal Government. The most significant thing about the Federal Reserve's operations in 1960 is not that they were extraordinary but, instead, that they were typical of Federal Reserve operations under the flexible monetary policy that has been in effect now for a full decade.

That policy, as I have capsuled it before in the shortest and simplest description I have been able to devise, is one of leaning against the winds of inflation and deflation alike--and with equal vigor.

It is, in my opinion, the policy that the Federal Reserve must continue to follow if it is to contribute to the provision of conditions conducive to a productive, actively employed, growing economy with relatively stable prices.

Yet, while the necessity for adhering to that policy remains as great as ever, the difficulty of executing it has become vastly greater. This is so because of economic and financial cross-winds that have been developing for years and, since mid-1960, have been gaining in force.

The problem, it now appears, and it is by no means a problem for monetary policy alone, is to lean against cross-winds--simultaneously. I do not know how effectively this can be done. I do know, however, that it will not be easy--just as the problems of monetary policy and of other financial policy have never been easy.

To put in perspective the problems that the Federal Reserve faces today--and how it is adapting to this problem--let me briefly review monetary policy over the past 20 years.

Immediately upon the United States' entry into World War II in December 1941, the Board of Governors announced that the Federal Reserve was prepared--

> 1. "To use its powers to assure that an ample supply of funds is available at all times for the war effort, and
>
> 2. "To exert its influence toward maintaining conditions in the United States Government security market that are satisfactory from the standpoint of the Government's requirements."

Making good on its words, the Federal Reserve saw to it that the banking system was supplied with ample lendable reserves to provide the Government with all the war-financing funds that it could not raise through taxation and through borrowing people's savings.

It did so by buying outstanding Government securities on a huge scale. The Federal Reserve's payments for these securities wound up in bank reserves. In turn, the banking system used these additional reserves to purchase new securities that the Treasury was issuing to obtain further funds to finance the war effort.

To keep the process going, the Federal Reserve in effect maintained a standing offer to buy Government securities in unlimited amount at relatively fixed prices, set high enough to assure that their interest rates or yields would be pegged at pre-determined low levels. When no one else would accept those yields and pay those prices, the Federal Reserve did so. And in so doing, it helped to finance the war.

The process was successful for its emergency purpose. But the procedure of pegging Government securities at high prices and low yields entailed a price of its own that the economy--the people and the Government alike--would later have to pay. The results were two-fold:

1. During wartime, money was created rapidly and continually, in effect setting a time bomb for an ultimate inflationary explosion--even though the immediate inflationary consequences were held more or less in check by a system of direct controls over prices, wages, materials, manpower, and consumer goods.

2. The market for Government securities became artificial. The price risks normally borne by participants in that market were eliminated: bonds not payable for 20 years or more became the equivalent of interest-bearing cash since they could be turned into cash immediately at par value or better--at the option of the owners, at any time.

The pegging of yields and prices of Government securities was continued for some time after the war to provide a gradual transition to a market freely responsive to the changing demand for and supply of securities. A gradual transition was especially important because capital values generally had become moored to the artificial yields and prices in the pegged market for Government securities.

By 1950, however, the need to end the dependence of the Treasury and the Government securities market upon money creation by the Federal Reserve, and to halt the inevitable inflationary consequences, had become clear to many observers. The outbreak of hostilities in Korea and the inflationary crisis that accompanied it brought the matter to a head.

Understanding of the problem was enhanced by an exhaustive investigation conducted by a Special Subcommittee of the Joint Congressional Committee on the Economic Report, under the chairmanship of Senator Paul Douglas. In its report in January 1950, the Congressional Subcommittee said means must be found for discontinuing the pegging of the Government securities market--if financial stability and effective control over the creation of new money were to become possible in the decade of the 1950's.

After considerable negotiation, the Treasury and the Federal Reserve System reached an Accord, jointly announced by them on March 4, 1951, that served to recognize and reaffirm that:

1. To serve the public welfare, Federal Reserve policy must be directed toward maintaining monetary conditions appropriate for the economy as a whole, rather than toward special treatment for the Treasury and the Government as if their interests could differ properly from those of the people as a whole.

2. Likewise to serve the public welfare, the Treasury's borrowing operations in management of the Government's debt must be reasonably calculated to induce loans to the Government in an economic system where no one can be compelled to lend his money at interest rates that he would be unwilling to accept voluntarily.

Thus, the Accord re-established the complementary operation of monetary and debt management policies: by the Federal Reserve, to regulate the availability, supply, and cost of money with a view to its economic consequences; by the Treasury, to finance the Government's needs in the traditional context of a competitive market.

To provide for the gradual withdrawal of the pegs that had fixed market prices and yields, several procedures were instituted immediately and carried out over the next weeks and months.

That's much easier to say now than it was to do then. For this was the danger:

1. Hanging over the market like a storm cloud were two issues of the longest term, 2-1/2 per cent bonds, outstanding in the total amount of $19.7 billion. Their prices had been propped around 100-3/4 throughout January and February 1951, by price-supporting purchases.

2. Although these bonds were not due for redemption until 1967-72, they were instantly saleable in markets. In fact, many of their holders were exercising their right to sell--and selling in large amounts--so as to reinvest the proceeds in private securities yielding a higher return.

3. Even a lowering of the price props, much less a complete withdrawal, might very easily cause holders of these instantly marketable

securities to unload them on the market so heavily as to cause a collapse in the market that might, in turn, provoke a sharp economic setback.

Since the primary necessity was to safeguard the market and the economy against that danger, these were the first steps taken under the Accord:

Holders of the overhanging, fully marketable 2-1/2 per cent bonds of 1967-72 were offered an opportunity to exchange them, in early April 1951, for 2-3/4 per cent bonds of 1975-80 that could not be sold at all although they could, at the holder's option, be converted into 1-1/2 per cent notes carrying sale privileges.

While the exchange was being effected, support buying was continued by the Federal Reserve and the Treasury, but at declining prices: from January through April, net purchases by the Federal Reserve totaled approximately $1.4 billion. When the exchange was completed, the offer of nonmarketable bonds had been accepted on a scale sufficient to remove from the market $13.6 billion of the overhanging marketable bonds, including $5.6 billion that had been held by the Federal Reserve and the Treasury.

This exchange paved the way for discontinuance of Federal Reserve purchases of Government bonds in support of their prices.

In May and June, net purchases by the Federal Reserve of long-term bonds dropped off to $250 million, but that was enough to assure against development of disorderly conditions in the market. After that, the Federal Reserve ceased buying almost altogether: purchases during the entire last half of 1951 totaled only $20 million. And prices, which had been supported around 100-3/4 at the start of the year, fluctuated around 97 during the last half of the year when the bond market was on its own.

As the years 1951 and 1952 progressed, however, market developments demonstrated a disturbing skepticism among investors that the Federal Reserve was in fact abstaining (or would continue to abstain) from attempting to maintain certain predetermined interest rates, regardless of the over-all state of the demand for and the supply of savings. This skepticism was fed by market observation that the System engaged in purchases of securities involved in Treasury financings around the periods of such financings.

After very careful study of the functioning of the Government securities market and of the relation of Federal Reserve monetary operations to the market, the System decided that it would limit its open market transactions to short-term securities, usually those of the very shortest term: Treasury bills. It also decided to refrain from operations in securities involved in Treasury financings. In taking these steps, the Federal Reserve objective was to convince the market that it was not undertaking to peg interest rates--and most certainly not those on intermediate- and long-term securities.

Accordingly, to minimize market uncertainty as to possible Federal Reserve operations affecting market rates, and thereby to aid the effective competitive functioning of the market, the System announced in April 1953 that until further notice, unless disorderly conditions arose in the market, it would operate only in the short-term area, where its operations would have the least market impact.

I think I should point out here, in fairness to my colleagues on the Federal Open Market Committee, that in this decision to limit our open market operations to the short end of the market, we were not unanimous--neither then, nor since then.

Indeed, the divergence of views in the System on this question has been more marked and more continuous than on any other that I can recall in my ten years in the Federal Reserve. That, I think, is readily understandable because the question relates to the techniques of open market operations--a highly technical and involved subject--rather than to general credit policy itself.

In my opinion, it is and always will be easier to achieve full agreement on what to do than on how to do it. To me, that explains why the uninterrupted character of the divergence in the System over operating techniques contrasts sharply with the rather high degree of agreement we have had, most of the time, over questions of general credit policy--whether and when to ease or restrain, and how much. Also, why it contrasts completely with the undeviating firmness of our opposition, at all times, to returning to a pegged market.

These matters, however, are too well known to members of this Committee for me to labor them further at this point: the records of your past hearings, as well as our Annual Reports, contain the views on that score of several members of the Open Market Committee, including the former and the present vice chairmen of our Committee, Messrs. Allan Sproul and Alfred Hayes of the Federal Reserve Bank of New York, as well as myself as chairman.

In any event, following the 1953 decision I have described--the decision to confine our open market transactions to the short-term sector of the market--the emphasis in Federal Reserve operations continued to be placed upon providing bank reserves to meet the economy's needs rather than to set particular rates of interest. Inevitably, however, interest rate movements, since they reflected basic demand and supply conditions, continued to be one of many factors considered by the Federal Reserve in making judgments about the need for changes in the reserve base. Conversely, Federal Reserve operations in the market continued, inevitably, to be an important influence affecting the general level of market interest rates.

Despite confinement of its operations ordinarily to the short-term area, the Federal Reserve stood prepared to buy securities other than Treasury bills should unusual developments create disorderly conditions in the Government securities market and thus in credit markets as a whole. When disorderly conditions seriously threatened as in late November of 1955 or actually developed as in the summer of 1958, the Federal Reserve bought longer term securities to maintain or re-establish orderly trading. Apart from these exceptional and infrequent circumstances, however, the Federal Reserve maintained its reliance upon operations in Treasury bills without interruption until 1960. With the introduction of the 6-month Treasury bill in 1958 and the 12-month Treasury bill in 1959, the System extended the maturity range of its operations within the short-term area.

Toward the close of 1959 there were increasing indications, signaled by rapid rises in market interest rates accompanying a mounting intensity of borrowing demands, that conditions bordering on the disorderly might be encountered increasingly in the future and that there might be more occasions than in the past for corrective operations by the Federal Reserve in maturities beyond the range of Treasury bills.

After the middle of 1960, another consideration pointing to a possible need for Federal Reserve operations in longer term securities arose from the convergence of two important developments.

1. On the domestic front, a decline in key sectors of business activity, accompanied by gradual rise in unemployment, suggested that the economy might be moving downward on a broad pattern of recession.

2. In the area of international financial accounts, a big deficit in the U. S. balance of payments was made larger by a substantial outflow of short-term funds from the United States to foreign money centers, partly in response to higher interest rates abroad.

As I stated earlier, the Federal Reserve had been making bank reserves available to ease the credit situation since the winter of 1960. Thus, it had been a contributing influence in the decline in market interest rates to mid-1960. In the light of the domestic business and employment situation and the balance of international payments deficit, this decline presented us with a dilemma in the latter part of 1960.

If the Federal Reserve continued to supply reserves by buying only Treasury bills, the direct impact of its purchases might drive the rate on those securities so low as to encourage a further outflow of funds to foreign markets and thus aggravate the already serious balance of payments deficit.

If, on the other hand, the Federal Reserve refrained from further action to supply funds for bank reserves because of the balance-of-payments situation, it would be unable to make its maximum contribution toward counteracting decline in domestic economic activity through the stimulative influence of credit ease.

Thus, in an effort to expand reserves and yet to minimize the repercussions on the balance of payments, the Federal Reserve began, in late October 1960, to provide some of the additional reserves needed by buying certificates, notes, and bonds maturing within 15 months. Since that time, the System has bought and sold such securities, in addition to bills, on a number of occasions, duly reporting these portfolio changes in a public statement issued every Thursday.

Now here let me note something about the decline in interest rates that took place in 1960. During the first eight months, market rates on Treasury bills and intermediate-term issues fell much more sharply than on bonds; as is usual in a period of declining rates.

After late summer, however, the differential between short- and long-term rates ceased to widen, and the average level of rates itself remained relatively unchanged. The increased net outflow of domestic and foreign capital from the United States in the second half of the year, in response partly to the attraction of higher interest rates and potential capital gains abroad, was itself a factor in keeping interest rates in the United States from declining, because it reduced the supply of funds available here.

It was in the latter part of 1960, as I have noted, that Federal Reserve operations were directed more and more toward reducing the direct impact on Treasury bill yields of Federal Reserve purchases. Thus, when the System was providing for the large seasonal expansion in credit needs that occurs in the fall and pre-Christmas seasons, it did not rely solely on further open market purchases but took actions that made vault cash holdings of banks fully available for meeting reserve requirements. And on the occasions when the System did engage in open market operations, it often conducted these operations in short-term Government securities other than Treasury bills.

With the domestic economy and the balance of payments continuing to pose conflicting problems, open market transactions in securities other than Treasury bills are continuing. Beginning on February 20, as we stated in an announcement issued on that date, a copy of which is attached to this statement, the Federal Reserve has engaged in purchases of securities having maturities beyond the short-term area, putting to practical test some matters on which it has been possible in recent years only to theorize.

There is still a question as to the possibility of bringing about a meaningful decline in longer term rates through purchases of longer term securities without, at the same time, causing a shift in market demand toward short-term securities that would also press down levels of short-term rates.

On the other hand, it seems to me, few could question the desirability of the result, if it can be attained, as a means of keeping financial incentives attuned to the current needs of our domestic economy and our international financial position.

We will want to observe closely, of course, the effect of this change in operating techniques on the market and its capacity to fulfill its role in transferring a large volume of securities among our various financial institutions to facilitate their responses to shifts in the supply of savings and the demands of borrowers.

In our country, the Government cannot force anyone to lend his money at rates he is unwilling to accept--any more than it can force him to spend his money at prices he is unwilling to pay. In the securities market, investors always have the alternative of investing their funds in short-term securities if they feel that yields in the longer-term area are unfavorable. Therefore, in the outcome of this test much will depend on the reactions of investors.

As I have said many times in the past, before this Committee and others, I am in favor of interest rates being as low as possible without stimulating inflation, because low rates can help to foster capital expenditures that, in turn, promote economic growth.

Yet, as I assume we can all agree, interest rates cannot go to and long remain below the point at which they will attract a sufficient volume of voluntary saving to finance current investment at a relatively stable price level. At least we can agree, I think, that interest rates cannot be driven and long held below that point without resort to outright creation of money on such a scale as to invite inflation, serious social inequity, severe economic setback, and, under present conditions, an outflow of funds to other countries and consequent drains on this country's gold reserves.

I do not believe anyone expects the Federal Reserve to engage in operations that will promote a resurgence of inflation in the future. In combating inflation in the past, undue reliance has perhaps been placed on monetary policy. I can readily agree with those who would have fiscal policy, with all of its powerful force, carry a greater responsibility for combating inflation, and I am encouraged to think that this may be likely in the future. If we do this, we should more nearly achieve our over-all stabilization goals, along with some reduction in the range of interest rate fluctuation.

That, however, is a matter for another day. Today, we have in this country a serious problem to contend with in the erratic but persistent rise in unemployment that has taken place since mid-1960. In January, the seasonally adjusted rate of unemployment was 6.6 per cent of the labor force, the highest percentage since 1958; the actual number of persons unemployed was 5.4 million, the highest number since the days before World War II.

The contracyclical operations that the Federal Reserve is and has been conducting, despite the handicaps imposed by the balance of international payments difficulties that we hope will be overcome, should be helpful, as they have been in the past, in combating that part of unemployment caused by general economic decline. Certainly we mean them to be.

While the unemployment that arises from cyclical causes should prove only temporary, there are, however, forces at work that have produced another, structural type of unemployment that is worse, in that it already has proved to be indefinitely persistent--even in periods of unprecedented general prosperity.

The problem of structural unemployment is manifest in the higher total of those left unemployed after each wave of the three most recent business cycles, and in the idleness of many West Virginia coal miners, Eastern and Midwestern steel and auto workers, West Coast aircraft workers, and like groups, in good times as well as bad.

To have important effect, attempts to reduce structural unemployment by massive monetary and fiscal stimulation of over-all demands likely would have to be carried to such lengths as to create serious new problems of inflationary character--at a time when consumer prices already are at a record high.

Actions effective against structural unemployment and free of harmful side effects therefore need to be specific actions that take into account the who, the where, and the why of unemployment and, accordingly, go to the core of the particular problem.

Analysis of current unemployment shows that, in brief:

1. The lines of work in which job opportunities have been declining most pronouncedly for some years are farming, mining, transportation, and the blue collar crafts and trades in manufacturing industries.

2. The workers hardest hit have been the semi-skilled and the unskilled (along with inexperienced youths newly entering the labor market). These workers have accounted for a significant part of the increase in the level and duration of unemployment. Among white collar groups, employment has continued to increase and unemployment has shown little change even in times of cyclical downturn.

3. The areas hardest hit have been, primarily, individual areas dependent upon a single industry, and cities in which such industries as autos, steel, and electrical equipment were heavily concentrated.

Actions best suited to helping these groups would appear to include more training and re-training to develop skills needed in expanding industries;

provision of more and better information about job opportunities for various skills in various local labor markets; tax programs to stimulate investment that will expand work opportunities; revision of pension and benefit plans to eliminate penalties on employees moving to new jobs; reduction of impediments to entry into jobs, and so on. Measures to alleviate distress and hardship are, of course, imperative at all times.

In some of the instances cited, the primary obligation of the Government will be leadership, rather than action, for obviously a major responsibility and role in efforts to overcome unemployment, both cyclical and structural, rests upon management and labor.

For our part, we in the Federal Reserve intend to do our share in combating the cyclical causes of unemployment, as effectively as we can, and in fostering the financial conditions favorable to growth in new job opportunities.

Meanwhile there is, I think, need on the part of all of us to recognize that the world in which we live today is not only a world that has changed greatly in recent years, but also a world that even now is in a period of further transition.

In economics and finance, no less than in other relationships, the lives of nations and peoples throughout the earth have been made more closely inter-linked by developments that have progressed since the beginning of World War II--inter-linked at such speed, in fact, as to outstrip recognition.

Today, the condition of our export trade, from which a very large number of Americans derive their livelihood, depends not only upon keeping competitive the costs and prices of the goods we produce for sale abroad, but also upon the prosperity or lack of it in the countries that want to buy our goods.

Whether our Government's budget is balanced or not, a factor that greatly affects our economic and financial condition, depends not only upon our own decisions respecting expenditures and taxes, but also upon decisions by governments abroad as to how far they will share the costs of mutual defense and of programs to aid underdeveloped nations of the world. The decisions those governments make affect, in turn, their budget positions and, through them, economic and financial conditions in their own countries.

Every country, of course, will always have problems of its own that differ from the current problems of other lands. Communist Russia, for example, gives some signs of worry over a problem old and familiar to us and to them: The danger of economically destructive inflation. The New York Times of January 30 reported that Premier Khrushchev, in a recent public speech, had pointed to precisely that danger, noting that "the purchasing power in the hands of the Soviet people might exceed the value of the goods available for them to buy."

In Brazil, a new administration is seeking means to cope with an inflation that already has exacted an enormous price in suffering inflicted upon her people by soaring increases in the cost of living.

In Belgium, a program of austerity, to bring about adjustments made necessary by the loss of the Congo, provoked riots that recently made headlines across the United States.

In the Free World, the United States has not been alone in finding that its domestic situation and balance-of-payments position seemed to call for conflicting actions, thus presenting monetary and fiscal policy makers some complicating cross-currents.

On January 19, for example, the German Federal Bank reduced its equivalent of our discount rate and made known at the time that it was doing so, despite the high level of activity in the German economy, for the purpose of reducing a heavy and troublesome inflow of funds from other countries. A month earlier the Bank of England had reduced its bank rate also, to curb a short-term capital inflow.

Over the last weekend, Germany and the Netherlands up-valued their currencies by nearly 5 per cent; these actions should help them to reduce the inflow of volatile capital.

The truth of it is that the major countries of the Western world, after a long and painful struggle in the wake of World War II to restore convertibility of their currencies, and thus to lay the necessary basis for interchanges that can enhance the prosperity of all, have succeeded--only to find that success, too, brings its problems.

Today, though currency convertibility does in fact make possible an expanding volume of mutually profitable interchanges among nations, it also makes possible dangerously large flows of volatile funds among the nations concerned--flows on a scale that could shake confidence in even the strongest currencies, and cause internal difficulties in even the strongest economies.

To the causes of these flows--differences in interest rates, conditions of monetary ease or tightness, budgetary conditions, and developments of any kind that raise questions and doubts about determination to preserve the value of a country's currency--we must remain alert and ready, willing and able to meet whatever challenge arises.

I, for one, am confident that we will meet such challenges as may come. Our opportunities for the future are more important than the problems they bring with them. Let us seize these opportunities, firmly and without fear.

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Board of Governors
of the
Federal Reserve System

For immediate release February 20, 1961

Below is a copy of a statement issued in New York today, for immediate release.

At the direction of the Chairman of the Open Market Committee of the Federal Reserve System, the following announcement was made today by the Manager of the System Open Market Account for the information of the public and all participants in the market for Government securities:

> "The System Open Market Account is purchasing in the open market U. S. Government notes and bonds of varying maturities, some of which will exceed 5 years.
>
> "Price quotations and offerings are being requested of all primary dealers in U. S. Government securities. Determination as to which offerings to purchase is being governed by the prices that appear most advantageous, i.e., the lowest prices. Net amounts of all transactions for System account will be shown as usual in the condition statements issued every Thursday.
>
> "During recent years transactions for the System Account, except in correction of disorderly markets, have been made in short-term U. S. Government securities. Authority for transactions in securities of longer maturity has been granted by the Open Market Committee of the Federal Reserve System in the light of conditions that have developed in the domestic economy and in the U. S. balance of payments with other countries."

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Briefing material

Feb. 3, 1961

To: Mr. Martin

Fm: Chas. Molony

Here's the core part of the Patman remarks I mentioned as noteworthy -- for what he has to say about impact of FR bond purchases on short as well as long rates, and also for a clue to questions he may be asking you and other witnesses from his post as Chairman of the Joint Economic Committee.

Chas Molony

Original and 2 carbons attached

February 3, 1961

Representative Wright Patman, Congressional Record 25 January 1961, pages 1369-70, in the course of remarks on a tax measure introduced by him to "speed up substantially the rate at which business firms and farmers may write off... the cost of newly acquired machinery and equipment":

"... Much of the obsolescence with which we are faced today is as a direct result of the monetary policies of the Eisenhower administration and British bankers' thinking of 1810. The tight-money and high-interest policies have retarded investment, as indeed they were intended to do.

"Monetary Policies Paralyzed

"But monetary policies have not been the whole cause. Rather, the conclusion of business people and independent experts alike is that the real obsolescence period of most capital equipment today is a great deal shorter than the depreciation periods generally allowed under the tax laws. Some experts have estimated that if U.S. industry were actually replacing equipment as fast as it is becoming obsolete, the cost would be from $5 to $8 billion a year more than its present depreciation allowance.

"Plainly, no change in monetary policies likely to be made will be enough to correct the deficit which has accumulated over the long years of economic slumber. In truth, there are some disturbing signs that the new administration will itself be enmeshed in the Eisenhower monetary policies -- at least for some time to come. All policies I have heard suggested to date revolve around the notion that our first objective must be to preserve the gold. Thus the monetary policies which seem to be shaping up are modified by those of the past only by the notion that while short-term rates must continue to be held up - as a means of checking the flow of "hot funds" and easing the drain of our gold -- long-term rates can nevertheless be brought down and thus investment in new capital equipment can be allowed to resume.

"Over the past 6 years I have been, not the most effective critic, but very probably the most persistent critic, of the Federal Reserve's bills only policy. No one would be happier than I to see an end to that policy. But even if the bills only policy were completely eliminated, and the Federal Reserve officials became fully cooperative in the idea of trading in the long-term market, they could not make anything like the reduction in long-term rates that the economy calls for without also reducing short-term rates.

!' So, in context of the policies that seem to be shaping up, it is not too much to say that our balance of payments problem must be solved before any real solution to our domestic problems can be reached. Such a reduction in interest rates as the domestic economy clearly calls for does not seem to be in prospect. ....."

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date March 6, 1961

To Chairman Martin

Subject: Testimony note

From Ralph A. Young

RAY
WM

We have recorrected the paragraph on page 2 of your testimony as follows:

"In August also, and again in November, by actions taken in implementation of a 1959 Act of Congress, nearly $2 billion previously tied up in vault cash ~~and reserves~~ of member banks were released to assure ample coverage of heavy borrowing needs for the fall and pre-Christmas seasons. An additional $700 million was provided by further net purchases of U. S. Government securities."

The record of reserve requirement action shows that in August vault cash released amounted to $480 million and in November to $1.400 million, making a total of $1.880 million.

With the August action, reserve requirements of central reserve city banks were reduced by 1/2 per cent, providing $125 million in reserve funds. In connection with the November action, the reserve requirements were reduced by 1 per cent, providing $250 million. The November action raised the reserve requirements of country banks from 11 to 12 per cent absorbing $380 million. Thus the net provision of reserve funds by reserve requirement actions in August and November comes to a total of $5 million. This explains our subsequent deletion of "and reserves."

March 6, 1961

To Chairman Martin

From Jerome W. Shay

JWS

M

Subject: Your appearance before Joint Economic Committee on Tuesday, March 7.

Some possible questions that you may be asked during the hearing on Tuesday are listed below:

Open Market Operations in Long-term Securities

1. On what date did the OMC decide to take the action announced in the Press Release of February 20, 1961?

2. How did the various OMC members vote on the action announced on February 20?

3. How was the OMC directive modified to provide for the action announced on February 20?

(Congressman Reuss has indicated that he might be interested in the above questions.)

Bank Earnings

1. How does one account for the recent "unusually high" earnings of commercial banks?

2. Why haven't commercial bank loan rates come down more during recent months?

(Senator Fulbright has shown some interest in questions such as these.)

Bank Mergers

Mr. Hackley is furnishing you a memo on this matter which I mentioned to you recently.

The "Triffin Plan"

You may be asked for your views on such plans as those of Robert Triffin and E. M. Bernstein for the internationalization of reserves, et cetera. You may recall that about a year ago, in answer to a letter from Senator Douglas, we merely indicated that the Board's staff was following the plans. Congressman Reuss has indicated dissatisfaction with our letter to Douglas. Senator Butler seems to think any such plan might, in effect, devalue the dollar.

OECD

1. How do you or the Board look upon the OECD?

2. Might not the OECD, if put into operation, have some effect on the Board's independence?

(Senator Fulbright, or possibly other Committee members, may raise questions along these lines.)

Gold Outflow

You may recall that Senator Proxmire, now a member of the Committee, has pressed Senator Robertson for an investigation of the gold outflow and balance of payments problems and has said Congress should conduct such an investigation even if the Administration may not be sympathetic to it. Proxmire might open up a broad range of questions on this, including, for example:

1. Is the 25 per cent gold reserve requirement necessary?

2. Would the Board's authority under section 11(c) of the Federal Reserve Act to suspend such requirement be of any real value if the gold outflow should get worse?

3. Do any other foreign countries of importance have a gold reserve requirement? (Attached is a tabulation of the situation on this matter in selected foreign countries, prepared in Arthur Marget's division.)

GOLD AND FOREIGN EXCHANGE COVER REQUIREMENTS OF SELECTED FOREIGN CENTRAL BANKS

Central bank of	Liabilities against which gold or foreign exchange reserves are required	Required reserves (per cent) In gold	Required reserves (per cent) In gold or foreign exchange	Status of reserve requirements; recent changes; qualifying provisions
Argentina	Notes and demand liabilities	--	25	Suspended since October 1949. Only net foreign exchange holdings may be included. Gold cover requirement of 20 per cent eliminated by 1957 legislation.
Australia	--	*	*	
Belgium	Notes and demand liabilities	33-1/3	--	In effect since April 12, 1957. Previous legislation, which had been suspended from May 1, 1944, required a 30 per cent cover in gold and 40 per cent in gold or foreign exchange.
Brazil	Notes	--	25	In effect (but note qualification). Basis of requirement significantly reduces ratio of cover of total outstanding notes. Currency is issued exclusively by Treasury, which can either put it into circulation directly itself, or under "general legislation," i.e. through Rediscount Department or the Bank Loan Fund of Bank of Brazil. Gold and foreign exchange cover requirement applies only to currency issued under latter of the two methods. A large part of notes in circulation was put into circulation directly by the Treasury.

*No minimum requirement of gold or foreign exchange.

Central bank of	Liabilities against which gold or foreign exchange reserves are required	Required reserves (per cent) In gold	In gold or foreign exchange	Status of reserve requirements; recent changes; qualifying provisions
Canada	--	*	*	Unless the Governor in Council otherwise prescribes, Bank of Canada is not required to maintain gold or foreign exchange reserves in any minimum or fixed ratio to its liabilities. (Section 25 of Currency, Mint and Exchange Fund Act of 1952.) Section 26 of Bank of Canada Act of 1934 had specified reserve of not less than 25 per cent of note and deposit liabilities, to be held in gold coin or bullion, net amounts of specified types of foreign exchange, and specified quantities of newly-mined Canadian silver. This requirement was suspended from 1940 until 1952, when suspense procedure was superseded by Section 25 of Currency, Mint and Exchange Fund Act cited above.
France	Notes and other demand deposits	35	--	Suspended since September 1, 1939, by decree. Statutory requirement of a 35 per cent reserve in gold bullion or gold coin had been in effect only from June 1928. Previous legislation generally stipulated that Bank of France metallic reserve must at all times be adequate "to assure full convertibility" of note issue.
Germany	--	*	*	

*No minimum requirement of gold or foreign exchange.

Central bank of	Liabilities against which gold or foreign exchange reserves are required	Required reserves (per cent) In gold	Required reserves (per cent) In gold or foreign exchange	Status of reserve requirements; recent changes; qualifying provisions
India	Notes	1.15 billion rupees	5.15 billion rupees	In effect; requirement established in 1956. Foreign exchange assets must total at least 4 billion rupees and may be in the form of deposits abroad, foreign government securities maturing within five years, and bills of exchange bearing at least two good signatures and maturing in not more than 90 days, provided that these claims are payable in the currencies of countries which are members of the International Monetary Fund. At least 85 per cent of the gold must be held in India. The minimum amount of foreign exchange required may be lowered temporarily from 4 to 3 billion rupees by Cabinet action. Previously, Reserve Bank was required to maintain gold and foreign exchange reserves equal to at least 40 per cent of note issue, and at least 400 million rupees of such reserves had to be in gold.
Italy	Notes and other demand liabilities	--	40	Suspended since July 22, 1935. Requirement had been established by a decree-law of December 21, 1927.
Japan	--	*	*	
Netherlands	Notes, drafts, deposits, and other current account balances	--	50	In effect. Under Royal Decree of June 27, 1956, issued in conformity with Article 2 of decree of January 11, 1956, requirement is 50 per cent in gold and convertible foreign exchange; may be changed at any time by Royal Decree. Except in period 1914-1929, when requirement was 20 per cent in gold coin and bullion, required cover from 1860's to 1949 was 40 per cent in gold coin and bullion; this was suspended in 1940 and abrogated in 1945.

*No minimum requirement of gold or foreign exchange.

Central bank of	Liabilities against which gold or foreign exchange reserves are required	Required reserves (per cent) In gold	In gold or foreign exchange	Status of reserve requirements; recent changes; qualifying provisions
Sweden	Notes	150 million kronor	--	In effect. Requirement specified in Sveriges Riksbank Act of June 30, 1934, as amended to May 22, 1959. (See Chapter III, Article 11, which states gold reserve may not remain below this figure.) In addition, the Riksdag establishes a ceiling on the note-issuing authority of the Bank. In June 1960, total notes outstanding amounted to 6,800 million kronor; minimum gold reserve of 150 million is less than 2.2 per cent of this amount.
Switzerland	Notes	40	--	In effect since 1905. Requirement is currently in force under Article 19 of Federal Law on the Swiss National Bank, December 23, 1953.
Union of South Africa	Notes and other liabilities, including notes of other banks for which it has assumed liability under Section 15 of Currency and Banking Act	25	--	In effect. Requirement established by October 1948 amendment to Reserve Bank Act of 1944. In computing the reserve ratio the Reserve Bank may deduct from its liabilities an amount equal to the book value in Union currency of its assets outside the Union. Minister of Finance may suspend reserve requirement for 30 days, subject to extension by him for "periods" not exceeding 15 days each. (Language of Section 17 of Reserve Bank Act of 1944, as amended by Section 9 of Act No. [illegible] of 1948.) From May 1944 to October 1948, required reserve was 30 per cent in gold coin and bullion against notes only. Between 1920 and 1944, requirements were 30 per cent in gold against notes, and 30 per cent in gold and specie against deposits and bills payable; silver specie was limited to one-fifth of latter reserve.

Central bank of	Liabilities against which gold or foreign exchange reserves are required	Required reserves (per cent) In gold	In gold or foreign exchange	Status of reserve requirements; recent changes; qualifying provisions
United Kingdom	Notes in excess of £ 2,350,000,000	100	--	In effect. From 1844 to 1928, an increase in note issue had to be matched by a corresponding increase in Bank of England gold holdings. Since 1928, Bank has been required only to hold gold coin and bullion to the full value of notes in excess of a specified total fiduciary issue. Current applicable legislation: Section 2(1) of Currency and Bank Notes Act of 1954. Current fiduciary ceiling of £ 2,350 million established by U.K. Treasury in 1960, under legislation permitting it to establish for two years, and renew for another two years, ceiling above that laid down by Parliament. As of December 14, 1960, notes covered by gold amounted to £364,976.

Prepared by the Division of International Finance,
Board of Governors of the Federal Reserve System,
March 2, 1961.

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Date March 3, 1961

To Chairman Martin

From *Ralph A. Young*

A briefing note on proposals for the modification of the IMF. If questioned, you could even read this into the record.

Attachment

Proposals for Modification of the
International Monetary Fund in Relation
to International Capital Movements

To the extent that it is found impossible or inconvenient to avoid excessive international capital movements, thought must be given to methods for preventing such capital movements from disturbing the international payments system and thus the United States domestic economy. In particular, thought has been given to the possible improvement of the procedures of the International Monetary Fund in this respect. For this purpose, two types of proposals are apparently under consideration.

The first (typified by the so-called "Bernstein proposals") would have the Fund use its existing power to borrow currencies of its member countries and to lend such currencies to other members over and above their quota. For instance, if the United States wanted to offset a movement of capital to Germany, the Fund would borrow the corresponding amount of German currency and lend it to the United States; the United States could use that currency to redeem the dollar funds that had been transferred to the German central bank.

Such an operation might be more acceptable to Germany than a direct loan of German marks to the United States, because under the Articles of Agreement of the International Monetary Fund all sums made available to the Fund, as well as all sums owed to the Fund, are guaranteed against changes in their gold value. Sums loaned to the Fund would therefore be as free from the risk of depreciation as would physical holdings of gold, and they would have the advantage of yielding a return.

While the United States could borrow from the Fund without the need for special legislation, it is prevented from making loans to the Fund without Congressional action (Bretton Woods Agreement Act, Section 5). Obviously, foreign countries would be reluctant to make loans to the Fund for relending to the United States unless they could be assured that if they needed dollars in the future, the United States would be prepared to make similar loans available to the Fund. For this reason, this proposal is likely to remain impractical unless the Congress authorizes U. S. loans to the Fund.

The second proposal (exemplified by the Triffin plan) envisages the deposit with the Fund of foreign currencies which a country acquires over and above the amounts it wishes to hold itself. For instance, if there were a flow of capital from the United States to Germany and Germany did not want to keep the funds invested in dollars, it could deposit them with the International Monetary Fund. Again, the benefit for Germany would lie in the automatic guarantee of these deposits against any risk of depreciation in terms of gold.

In comparison with the first proposal, the second would have the disadvantage that the amount of funds involved would not be under the control of the United States. Under the first proposal, it would always be up to the United States to decide whether or not to borrow foreign currencies from the Fund, and thus how far to permit funds to be subjected to the automatic gold value guarantee. Under the second proposal, the decision on the amount involved would be entirely up to the creditor countries and to the management of the Fund.

At present most experts within the United States Government agencies and most executive directors of the Fund favor the first plan--that is, borrowing from the Fund--over the plan of permitting foreigners to deposit dollars.

Federal Reserve Position on Proposals with Respect to the Modification of the International Monetary Fund

The Staff Committee of the National Advisory Council on International Monetary and Financial Problems extensively discussed the attitude to be taken by the U. S. Executive Director of the International Monetary Fund in the preliminary exchanges of views among the Executive Directors on proposals to increase the effectiveness of the Fund. Staff members of the Board of Governors took part in these discussions. Studies are continuing and when conclusions are reached they will be made available through appropriate channels.

March 3, 1961.

S E L E C T E D F I N A N C I A L F A C T S

Series	Unit	Date	Latest period	Pre-ceding period	Year ago	Per cent change from: Preceding period	Year ago
MONEY AND CREDIT							
Consumer, total	Billions	Jan. '61	$55.0	$56.0	$51.5	- 1.8	6.8
Consumer, instalment	"	"	42.8	43.3	39.7	- 1.2	7.8
Mortgage debt outstanding, total	"	Q.3-'60	202.8	198.5	186.7	2.2	8.6
Mortgage debt, 1-4 family houses	"	"	139.1	136.1	128.0	2.2	8.7
Corporate securities issues, new capital	Millions	Q.1-'61	1/ 1,650	2,709	2,151	-39.1	-23.3
State and local gov't. issues, new capital	"	"	1/ 1,975	1,322	1,943	49.4	1.6
Total bank credit 2/	Billions	1-25-61	195.8	197.9	185.6	- 1.1	5.5
Total loans 2/	"	" " "	112.7	115.8	107.4	- 2.7	4.9
Investments	"	" " "	83.1	82.1	78.3	1.2	6.1
Business loans at city banks	"	" " "	31.2	31.9	29.8	- 2.2	4.7
Money supply 3/	* "	Feb. '61	141.3	140.2	141.1	0.8	0.1
Time deposits at commercial banks	* "	1-25-61	72.3	71.6	65.7	1.0	10.0
Liquid assets 4/	* "	Jan. '61	397.6	395.4	389.2	0.6	2.2
Turnover rates, 337 reporting centers	* Annual rate	Jan. '61	25.8	25.1	25.1	2.8	2.8

For footnotes, please see page 2.

March 3, 1961

SELECTED FINANCIAL FACTS

Series	Unit	Date	Latest period	Preceding period	Year ago	Per cent change from: Preceding period	Year ago
STOCK PRICES							
Common stock prices, Standard & Poor's	1941-3 = 10	Feb. '61	62.17	59.73	55.78	4.1	11.5
INTEREST RATES			Monthly average of daily figures			Change in basis points 5/	
91-day Treasury bills	Per cent	Feb. '61	2.42	2.24	3.96	18	-154
6-month " "	" "	"	2.60	2.47	4.30	13	-170
Intermediate term (3- to 5-year) issues	" "	"	3.54	3.53	4.66	1	-112
Long-term U. S. Gov't bonds	" "	"	3.81	3.89	4.22	- 8	- 41
Corporate AAA bonds (seasoned)	" "	Feb. '61	4.27	4.32	4.56	- 5	- 29
State and local AAA bonds	" "	"	3.14	3.15	3.40	- 1	- 26
Common stock yields, Standard and Poor's	" "	Feb. '61	3.13	3.28	3.40	- 15	- 27

* Seasonally adjusted.
1/ Estimated.
2/ Excluding interbank loans.
3/ Average of daily figures, semi-monthly, first half data.
4/ Includes money supply, time deposits at commercial and mutual savings banks, savings and loan shares, U. S. Government savings bonds and U. S. Government securities maturing within one year.
5/ One basis point equals 1/100 of one per cent.

March 3, 1961.

S E L E C T E D   E C O N O M I C   F A C T S

Series	Unit	Date	Latest period	Pre-ceding period	Year ago	Per cent change from: Preceding period	Year ago
GROSS NATIONAL PRODUCT							
Total	* Annual rate, billions	Q.4-'60	$503.5	$503.5	$486.4	0.0	3.5
Final purchases	" " " "	"	506.5	503.0	481.7	0.7	5.1
Inventory change	" " " "	"	- 3.0	.6	4.7	--	--
Consumer expenditures	" " " "	"	330.8	328.3	319.6	0.8	3.5
Business fixed investment	" " " "	"	66.0	70.8	70.8	-6.8	-6.8
Net exports	" " " "	"	4.6	3.7	- .4	--	--
Federal government	" " " "	"	53.3	52.7	52.5	1.1	1.5
State and local government	" " " "	"	48.8	48.0	43.9	1.7	11.2
Gross national product in constant (1959) dollars:	" " " "	"	491.9	492.7	483.3	-0.2	1.8
INCOME							
Total personal income	" " " "	Jan. '61	406.3	406.9	395.7	-0.1	2.7
Wages and salaries	" " " "	"	271.0	271.4	268.2	-0.1	1.0
Farm income	" " " "	"	12.9	12.9	11.3	0.0	14.2
Transfer payments	" " " "	"	31.0	30.9	27.7	0.3	11.9
Total disposable income	" " " "	"	356.2	356.7	346.5	-0.1	2.8
Total personal income, in constant (1959) dollars:	" " " "	"	397.6	397.8	393.3	-0.1	1.1

* Seasonally adjusted.

March 3, 1961.

S E L E C T E D   E C O N O M I C   F A C T S

Series	Unit	Date	Latest period	Preceding period	Year ago	Per cent change from: Preceding period	Year ago
BUSINESS OUTLAYS, PROFITS, ETC.							
Plant and equipment outlays	* Annual rate, billions	Q.2-'61	1/ $33.8	1/ $34.4	$35.9	-1.7	-5.9
Corporate profits before tax	" " " "	Q.4-'60	2/ 41.5	41.5	44.8	0.0	-7.4
Manufacturers' inventories	* Billions	Jan. '61	53.5	53.6	53.3	-0.2	0.4
New orders for durable goods	" "	"	13.0	13.2	14.2	-1.5	-8.5
DISTRIBUTION							
Retail sales, total	" "	"	17.7	18.0	18.1	-1.7	-2.2
Department store sales	* 1947-49 = 100	Feb. '61	2/ 147	2/ 142	142	3.5	3.5
Department store stocks	" " "	Jan. '61	2/ 165	167	161	-1.2	2.5
Auto sales, domestic	* Annual rate, millions of cars	"	4.8	5.9	6.0	-18.6	-20.0
Auto dealer stocks	Millions of cars	2-10-61	1.0	1.1	0.9	- 0.1	11.1
PRODUCTION							
Industrial production, total	* 1957 = 100	Jan. '61	102	103	111	- 1.0	- 8.1
Consumer goods	" " "	"	111	112	116	- 0.9	- 4.3
Equipment, including defense	" " "	"	100	101	103	- 1.0	- 2.9
Materials	" " "	"	98	99	110	- 1.0	-10.9
Steel production	1957-59 = 100	"	2/ 77.9	70.8	146.1	10.0	-46.7
" "	Per cent of capacity	"	2/ 50.0	46.3	95.5	--	--
Auto production	* Annual rate, millions of cars	"	4.5	5.6	7.7	-19.9	-42.0

* Seasonally adjusted.
1/ Anticipated.
2/ Estimated.

March 3, 1961.

S E L E C T E D   E C O N O M I C   F A C T S

Series	Unit	Date	Latest period	Preceding period	Year ago	Per cent change from: Preceding period	Per cent change from: Year ago
CONSTRUCTION							
Total	* Annual rate, billions	Feb. '61	$54.4	$54.8	$54.9	- 0.7	- 0.9
Private, total	" " " "	"	37.3	37.9	39.7	- 1.6	- 6.0
Residential, nonfarm	" " " "	"	19.8	20.4	22.5	- 2.9	-12.0
Nonresidential	" " " "	"	10.7	10.7	10.2	0.0	4.[illegible]
Public	" " " "	"	17.1	17.0	15.2	0.6	12.5
Housing starts, total private	* Annual rate, thousands of units	Jan. '61	1,098	984	1,366	11.6	-19.6
LABOR MARKET							
Total employment 1/	* Millions of persons	Jan.'61	66.6	66.4	66.1	0.3	0.8
Nonagricultural payroll employment	" " " "	"	52.3	52.2	52.9	0.2	- 1.1
Manufacturing employment	" " " "	"	15.7	15.8	16.6	- 0.6	- 5.4
Nonmanufacturing employment	* " " "	"	36.7	36.4	36.3	0.8	1.1
Average weekly hours at factories	* Hours	"	38.7	38.3	40.4	1.0	- 4.2
Average hourly earnings at factories	" "	"	$ 2.32	$ 2.31	$ 2.29	0.4	1.3
Average weekly earnings at factories	" "	"	$89.64	$88.23	$92.38	1.6	- 3[illegible]
Civilian labor force 1/	* Millions of persons	"	71.5	71.1	69.8	0.6	2.4
Unemployment 1/	" " " "	"	4.7	4.8	3.7	- 2.1	27.0
Unemployment rate	* Per cent of civilian labor force	"	6.6	6.8	5.3	- 2.9	24.5

* Seasonally adjusted.
1/ Data include Alaska and Hawaii.

March 3, 1961.

SELECTED ECONOMIC FACTS

Series	Unit	Date	Latest period	Preceding period	Year ago	Per cent change from: Preceding period	Year ago
PRICES							
Wholesale, total	1947-49 = 100	Jan. '60	119.8	119.5	119.3	0.3	0.4
Farm and food	"	"	100.0	99.2	96.3	0.8	3.8
Industrial	"	"	128.1	127.9	128.8	0.2	- 0.5
Sensitive materials	"	"	102.6	103.1	110.4	- 0.5	- 7.1
Consumer, total	"	"	127.4	127.5	125.4	- 0.1	1.6
Goods	"	"	118.0	118.4	116.7	- 0.3	1.1
Services	"	"	151.7	151.4	148.2	0.2	2.4

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date March 6, 1961

To Chairman Martin

Subject:

From Arthur W. Marget

The attached memorandum, by Mr. Furth, was prepared somewhat hurriedly in order to enable you to use it as a briefing paper, if you choose to do so, for your appearance before the Joint Committee. The discussion of "special facilities" for foreigners is to be found on page 5.

awm

Attachment

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date March 6, 1961.

To Mr. Marget

From J. Herbert Furth

Subject: Speculative capital movements, balance of payments, gold transfers, and interest-rate differentials.

Short-term capital movements were important in the U.S. balance of payments deficit and in the decline in the U.S. gold stock during the second half of 1960 (see the attached table).

These movements can be explained in part by interest-rate differences between the United States and other financial centers, but in large part also by other factors, including (but not limited to) uncertainties as to the future gold value of the dollar.

Two types of policies have been proposed to prevent such movements from harming the international payments system and the U.S. economy: first, policies aimed at reducing the movements to tolerable proportions; second, policies aimed at neutralizing unfavorable effects of such movements as may nevertheless occur.

Importance of short-term capital movements in the second half of 1960

In the second half of 1960, U.S. exports of merchandise and services failed to cover what may be called "basic" U.S. payments (imports of merchandise and services, military expenditures, pensions and remittances, recorded outflow of long-term capital and U.S. economic aid) by a seasonally adjusted amount of $1-1/2 billion at an annual rate. This compares with a similarly computed deficit of $2 billion for the first half of 1960, and $4-1/2 billion for 1959.

The second half of 1960 also saw an outflow of recorded U.S. short-term capital and of unrecorded capital of $3-1/2 billion at an annual rate, in contrast to an outflow at an annual rate of less than $1 billion in the first half of 1960 and an inflow in 1959. These capital movements raised the deficit in the U.S. balance of payments (as conventionally computed) to an annual rate of $5 billion in the second half of 1960, while such flows contributed very little to the deficit in the first half of 1960, and actually reduced the deficit in 1959.

The influence of such capital movements on the deficit in the second half of 1960 was probably even larger than indicated by these figures because there is reason to assume that some of the flows included in long-term capital outflows actually represented speculative short-term transactions and because there usually is an inflow rather than outflow due to unrecorded transactions. At the very least, however, the short-term capital movements accounted for 70 per cent of the total deficit in that period.

Such movements played an even larger role in the drain on the U.S. gold stock during the second half of 1960. Withdrawals of foreign private holdings of liquid dollar assets may add to that drain although they do not affect the U.S. balance-of-payments deficit (as conventionally computed) since these holdings are already considered a liability in computing the U.S. international liquidity position. However, such withdrawals, by increasing foreign official at the expense of foreign private dollar holdings, result in gold transfers to foreigners whenever a foreign monetary authority decides to convert its dollar acquisitions into gold.

In the second half of 1960, foreign private short-term dollar holdings declined at an annual rate of $1 billion, while they had increased in the first half of 1960 and in 1959. The movement of private dollar holdings therefore reduced the impact of the U.S. deficit on gold movements in the previous periods, but increased that impact in the second half of 1960. In fact, if Germany had not taken most of its reserve gains in dollars, the decline in the U.S. gold stock in the second half of 1960 would have exceeded the balance-of-payments deficit, in spite of the U.S. purchase of gold from the International Monetary Fund.

As it was, the U.S. gold stock declined in that period at an unprecedented annual rate of $3 billion,as compared to a negligible decline in the first half of 1960, and a decline of $1 billion in 1959.

Causes of the short-term capital movements

The outflow of U.S. short-term and of unrecorded capital and the withdrawal of foreign dollar holdings was in part certainly due to the emergence of considerable differences between interest rates in the United States and in other financial centers, particularly the United Kingdom and Germany.

It is equally certain, however, that differences in interest rates did not account for all of the movements. First, there were large outflows to countries where interest rates were not higher than in the United States, such as the Netherlands and Switzerland. Second, part of the outflow to the United Kingdom resulted in private purchases of gold in the London free market; these purchases reached a record level in the second half of 1960.

Third, a large part of the funds moving to Germany were attracted by the expectation of an appreciation of the German mark instead of mere interest rate differentials; Germany prohibited interest payments to foreigners on short-term assets.

Fourth, movements of capital out of the United States in response to short-term interest-rate differentials were encouraged by developments in forward rates. The large outflow of capital from the United States forced the exchange rate of the dollar against the leading European currencies virtually to the floor represented by the "gold points", approximately 3/4 of 1 per cent below par. Under these conditions, the premium on forward dollars would have been expected to rise sharply, and largely to offset the attraction of higher interest rates abroad. It failed to do so as, for the first time since the war, some capital moved uncovered into foreign currencies.

Fifth, some capital apparently moved not into short-term but into long-term assets, obviously in the expectation of capital gains, which would result in the case of bonds from an expected decline in foreign interest rates and in the case of equities from the expectation of a continuing boom abroad, as contrasted with the expected recession in the United States. The importance of this factor is indicated by a reflux of capital to the United States in early 1961 to take advantage of expected advances in quotations at the New York Stock Exchange.

Sixth, some expansion of U.S. bank credit to foreigners and some repatriation of dollar holdings of foreign commercial banks were probably influenced by changes in relative credit demands and availabilities, and especially by a tightening of commercial bank reserve requirements in some foreign countries, independently of relative levels of money-market rates.

While there can be no doubt that all these factors played an appreciable role, it is virtually impossible at this time to make a reasonable quantitative estimate of their relative importance.

Avoidance of excessive capital movements

Large movements from dollars into gold or other currencies can basically be attributed to an excessive supply of dollars abroad. In the 2-1/2 years preceding the start of that movement in mid-1960, official and private liquid dollar holdings (short-term claims and holdings of U.S. Government bonds and notes) of foreign countries rose $4 billion. If it had not been for this increase, foreigners presumably would have been glad, in the aggregate, to keep not only existing assets but also moderate further receipts in the form of dollars: before 1958, foreigners used to complain about an international scarcity rather than an international glut of dollars.

As long as the "basic" balance of payments of the United States remains in long-term equilibrium, and the supply of dollars to foreigners therefore remains limited, even relatively large capital movements would be unlikely to result in a general "flight from the dollar." In principle, therefore, the best way to avoid excessive volatile capital movements will be to restore and preserve equilibrium in the "basic" balance of international payments of the United States.

Apart from this general consideration, excessive capital movements may be avoided by eliminating their specific causes.

(a) Those capital movements that are caused by uncertainty as to the future value of the dollar (reflected in movements into gold and in the failure of forward exchange rates to rise) can best (or only) be avoided by restoring confidence in the stability of the U.S. economy in general and of the U.S. dollar in particular.

Insofar as capital movements are due to attractive yields and expected capital gains connected with rapid rates of growth abroad, the best remedy is to make sure that economic growth in the U.S. provides similar attractions for capital investment at home.

(b) Capital movements exclusively caused by differences in short-term interest rates not offset by forward-exchange costs may be divided into two groups.

Some capital movements may result from "structural" differences in short-term interest rates, due to differences in the pattern of supply of and demand for funds in various money markets. It would be unrealistic to expect market interest rates to be as low in Japan as in the United States, and there is no economic need to prevent funds from moving out of countries in which the supply of short-term capital is ample to countries in which it is scarce.

The second (and more important) type of differences results from variations in the pattern of cyclical fluctuations. A country suffering from a recession does not (all other things being equal) have the same market rate of interest as a country experiencing a rapid upswing. Such movements, however, will not affect the long-term equilibrium in the balance of payments of the countries involved as long as it can be expected that the flows will be reversed when the relative cyclical positions of the countries are reversed.

Problems arise only when these structural and cyclical flows become so large as to impair confidence in the smooth working of the international payments system. In this case, several different methods of approach may be used.

The country suffering from a speculative outflow may try to keep its interest rates higher than the current structural or cyclical situation would warrant. It may do so by trying to keep all rates high, reducing the supply of funds throughout the economy. Such an attempt would obviously be economically and politically dangerous since it would almost certainly reduce economic activity, employment, and "real" national income.

The country may, instead, try to raise only those rates which appear to be particularly attractive to international capital. Assuming that such capital is primarily interested in short-term rates, this would mean an attempt to raise short-term rates while not raising, or actually lowering, medium or long-term rates. The success of such an operation depends not only on the power of the monetary and fiscal authorities to influence the supply of and demand for both long and short-term funds, but also on the flexibility of the money market, and especially the size and speed of arbitrage operations among different maturities.

Whenever arbitrage is effective, the success of the authorities in decisively changing interest-rate patterns is likely to be short-lived.

These difficulties may invite attempts at insulating interest rates for international transactions from the domestic level, either for all foreigners or only for foreign official accounts. It would be possible to issue special Treasury securities and to induce banks to offer special deposit rates, available only to foreigners, but to all foreigners. The main shortcoming of such a policy would be the difficulty of preventing domestic investors from transferring their funds to foreign institutions and thereby increasing almost infinitely the amount of "foreign" funds at the expense of "domestic" funds. If this happened, the attempt at insulation would break down, and domestic rates would tend to rise to the level offered to "foreign" holders.

This danger could be avoided if the special rates were restricted to foreign monetary authorities, especially if these authorities undertook not to make the advantage indirectly available to private holders. On the other hand, such a restricted measure would probably not have an appreciable effect on international capital movements, since major central banks do not decide on the division of their reserves among gold, sterling, and dollars on the basis of interest yields. Some of them, including those of the United Kingdom, Belgium, the Netherlands, and Switzerland, keep all their reserves, except for working balances, in the form of gold; in the second half of 1960 these four banks were responsible for two-thirds of all the gold purchases from the U.S. Treasury. Even small central banks do not seem usually to determine their gold policy on the basis of interest rates. At most, some of those banks might move funds from London to New York in response to higher interest rates. Competition between London and New York for central bank funds, through special rates offered regardless of market levels, might, however, threaten friendly cooperation between the two major central banking institutions of the free world. Moreover, the structural level of interest rates is usually higher in London than in New York and it would, therefore, be easier for London than for New York to offer particularly attractive discriminatory rates to foreign central banks.

The bulk of the funds invested by foreign central banks in the special securities or deposits, would presumably not be shifted out of gold or sterling, but out of other dollar assets. In this case the final effect of the special rates would again be felt in the domestic money market; moreover, the main result of the attempt at insulating the market for foreign monetary authorities would merely be to burden the balance of payments with higher interest payments to foreigners.

In any case, facilities for foreigners should be terminable whenever a change in the international or domestic financial position of the United States would make a continuing inflow of foreign funds no longer desirable or positively undesirable.

Avoidance of harmful effects of capital movements

If it were impossible or inconvenient to avoid large speculative capital movements, it still would be possible to prevent such movements from disturbing the international payments system and thus the U.S. domestic economy.

If the main capital movements are restricted to some major countries (as in the second half of 1960), it may be possible to conclude bilateral agreements under which these countries keep the inflowing private funds invested in dollars; in this case, the only effect of the capital movements would be to increase foreign official holdings at the expense of foreign or domestic private holdings of dollars, leaving the U.S. gold stock unchanged.

If such bilateral agreements are considered impractical, or if the foreign countries involved insist on conditions that would seem unacceptable, the same result may be achieved by means of existing international institutions, and in particular by utilizing present and perhaps also increased future resources of the International Monetary Fund.

Two types of proposals to increase the effectiveness of the Fund in this matter are currently under consideration. The first would use the Fund's existing power to borrow currencies of its member countries and to lend them to other members, regardless of quota limitations. For instance, if the United States wanted to offset a movement of capital to Germany, the Fund would borrow the corresponding amount of German currency and lend it to the United States; the United States could use that currency to repurchase the dollar funds that had been transferred to the German central bank. Germany would thus end up with increased claims against the Fund rather than increased holdings of either dollars or gold.

Such an operation might be more acceptable to Germany than a direct loan of German marks or dollars to the United States, because under the Articles of Agreement of the International Monetary Fund all sums made available to the Fund, as well as all sums owed to the Fund, are guaranteed against changes in their gold value. Sums loaned to the Fund would therefore be as free from the risk of depreciation as would physical holdings of gold, and they would have the advantage of yielding a return.

While the United States could borrow from the Fund without the need for special legislation, it is prevented from making loans to the Fund without Congressional action (Bretton Woods Agreement Act, Section 5). Obviously, foreign countries would be reluctant to make loans to the Fund for relending to the United States unless they could be assured that if they needed dollars in the future in excess of their Fund quota, the United States would be prepared to make similar loans to the Fund. For this reason, this proposal is likely to remain impractical unless the Congress authorizes U.S. loans to the Fund.

The second proposal envisages the deposit with the Fund of currencies other than its own which a country acquires over and above the amounts it wishes to hold. For instance, if there were a flow of capital from the United States to Germany and the German central bank did not want to keep the resulting reserves invested in dollars, it could deposit them (against interest) with the Fund. Again, the benefit for Germany would lie in the automatic guarantee of these deposits against any risk of depreciation in terms of gold.

In comparison with the first proposal, the second would seem to have the disadvantage that the amounts involved would not be under the control of the United States. Under the first proposal, it would always be up to the United States to decide whether or not to borrow foreign currencies from the Fund, and thus how far to permit funds to be subjected to the automatic gold value guarantee. Under the second proposal, the decision on the amount involved would initially be up to the creditor countries and to the management of the Fund.

Actually, however, the United States would be able, under the Articles of Agreement of the International Monetary Fund, to limit the amount of dollars deposited with the Fund by redeeming any excess in gold -- just as the United States would be able to avoid borrowing foreign currencies from the Fund under the first proposal by making gold payments to the foreign countries holding dollars.

Another disadvantage of the second proposal might be that deposits with the Fund, with their combination of gold value guarantee and yield, could prove so attractive to foreign central banks presently holding dollar reserves that larger amounts would be deposited with the Fund than otherwise would be presented to the United States for conversion into gold. This danger might be avoided by keeping interest rates on those deposits low in relation to the yields of investments in U.S. money markets.

At present, most experts within United States Government agencies and most Executive Directors of the Fund favor the plan of borrowing through the Fund over the plan of permitting foreign countries to deposit dollars with the Fund. Their preference is presumably based less on the economic differences between these proposals (which are small) than on the fear that the second proposal might lead to the fundamental change in the free world's system of international payments proposed by Professor Triffin.

Professor Triffin, who at present is Consultant to the Council of Economic Advisers, has urged the replacement of sterling and dollars as international reserve currencies by a newly created monetary unit to be administered by the International Monetary Fund, and has advocated the voluntary deposits of dollars (and sterling) by foreign countries with the Fund as a first step toward a realization of his plan. To those who believe that the Triffin plan is either premature or unworkable, or outright harmful to the interests of the United States, the deposit proposal would be acceptable only on the understanding that it was not to be interpreted as an endorsement of further moves in the direction of that plan.

CAPITAL MOVEMENTS AND GOLD TRANSFERS, 1959-60

	1960 1/ 2nd half p/	1960 1/ 1st half	1959 2/
	(Billions of dollars)		
1. "Basic" U.S. balance of payments deficit 3/	1.3	2.2	4.5
2. Plus: Outflow of recorded U.S. private short-term capital and unrecorded transactions (inflow: -)	3.4	0.7	-0.8
3. Equals "conventional" deficit	4.7	2.9	3.7
4. Plus: Outflow of foreign private short-term capital (inflow: -)	1.0	-0.9	-1.1
5. Equals: Change in gold and in dollar liabilities to foreign authorities 4/	5.7	2.0	2.6
6. Minus: Increase in foreign official dollar holdings 4/	2.6	1.7	2.0
7. Equals: net gold sales	3.1	0.3	0.7

1/ At annual rates (without seasonal adjustment)

2/ Excluding U.S. subscription to International Monetary Fund.

3/ Imports of goods and services, military expenditures, pensions and remittances, outflow of private long-term capital, and U.S. economic aid, minus exports of goods and services.

4/ Includes international institutions.

p/ preliminary.

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date March 6, 1961.

To Chairman Martin

Subject:

From Mr. Hackley

Hart

Mr. Shay has suggested that, at the hearing tomorrow before the Joint Economic Committee, it is conceivable that some question might be asked you regarding recent antitrust actions by Justice Department in the banking field. I thought you might like to have some briefing material on this subject.

Accordingly, there is attached for your information a brief statement regarding the two bank merger cases and the one holding company case in which Justice has recently instituted antitrust proceedings.

Attachment

Recent Justice Department Actions with
Respect to Bank Mergers and Holding Company Acquisitions

Bank mergers. - Recently, the Justice Department instituted Sherman Act proceedings with respect to the consolidation of The Philadelphia National Bank and the Girard Trust Corn Exchange Bank. Justice has instituted similar proceedings with respect to the consolidation of First National Bank and Trust Company and the Security Trust Company of Lexington, Kentucky.

Both of these mergers had previously been approved by the Comptroller of the Currency under the so-called Bank Merger Act of 1960. As required by that Act, the Board of Governors (as well as the Federal Deposit Insurance Corporation and the Justice Department) had made a report to the Comptroller on the competitive effects of the mergers.

As to the Philadelphia merger, the Board reported:

> "The proposed consolidation of two of the three largest banks in the area would substantially lessen both existing and potential competition. The resulting bank would obtain a dominant position, with attending competitive advantages, strongly adverse to the preservation of effective competition."

As to the Kentucky merger, the Board reported:

> "The proposed consolidation would result in the elimination of the fourth largest of the six banks in Lexington and in a substantial lessening of competition. It would result in a substantial concentration in one institution of banking resources and fiduciary business in Lexington and Fayette County."

In both cases, the Board expressed its views only as to the competitive effects; it did not make any recommendation as to whether the mergers should be approved. That decision rested solely with the Comptroller. Under the merger legislation, the Comptroller was required to consider not only the competitive effects but certain other factors, such as financial condition, management, prospects, and the needs of the communities involved. Even though the mergers may have had adverse competitive effects, it was within the Comptroller's discretion to approve the mergers if he found that such adverse effects were outweighed by other considerations so that, on balance, the mergers would be in the public interest.

Bank holding company case. - On March 2, 1961, the Justice Department instituted proceedings against Bank Stock Corporation of Milwaukee, charging that its acquisitions of stock of certain banks violated the Clayton Act. On January 25, 1961, the Board of Governors, acting pursuant to the Bank Holding Company Act of 1956, had approved the acquisition by Bank Stock Corporation of stock of Bank of Commerce, Milwaukee. The Board's action was based upon consideration not only of the competitive effects of the acquisition but also the other factors required to be considered under the Holding Company Act.

In this case, as in the merger cases, the Justice Department's action was based solely upon its consideration of the competitive effect of the transaction, the only consideration involved in the antitrust laws. The bank merger legislation of 1960 does not exempt bank mergers from the Sherman Act; and the Bank Holding Company Act of 1956 expressly preserves the application of the antitrust laws (both the Sherman and the Clayton Acts) to acquisitions of bank stock by bank holding companies even though approved by the Board of Governors.

3-6-61

Budget Estimates for Fiscal Years 1961 and 1962

The Budget presented by President Eisenhower on January 16 estimated that the administrative budget would be virtually in balance in the current fiscal year and would show a surplus of $1.5 billion in fiscal 1962. The cash budget was estimated to show surpluses of more than $1 billion in both years. The receipts and expenditures totals giving these results are shown in the table below. The breakdown of the administrative budget totals are shown in the table attached to this note.

Fiscal Year Totals, in billions of dollars

	1959 Actual	1960 Actual	1961 Mid-year Review	1961 Budget Document (1-16-61)	1962 Budget Document
Administrative budget					
Receipts	67.9	77.8	80.8	79.0	82.3
Expenditures	80.3	76.5	79.7	78.9	80.9
Surplus (+) or deficit (-)	-12.4	+ 1.2	+ 1.1	+ .1	+ 1.5
Cash budget					
Receipts	81.7	95.1	100.6	99.0	103.1
Payments	94.8	94.3	98.1	97.9	101.8
Surplus (+) or deficit (-)	-13.1	+ .8	+ 2.5	+ 1.1	+ 1.3

Estimates for Fiscal 1961

The budget surplus of less than $100 million estimated for the current fiscal year compares with a surplus of $1.2 billion realized in fiscal 1960 and a deficit of $12.4 in fiscal 1959. The estimated decline of $1.1 billion in the surplus from the preceding year reflects a $2.4 billion increase in expenditures and a $1.2 billion increase in receipts.

Most of the rise in revenues is due to an increase, estimated at $2.6 billion, in receipts from individual income taxes. This rise reflects mainly the higher level of personal income reached in the second half of calendar year 1960 and the assumption that incomes will advance further in the current half year. Specifically, it is assumed that personal income in calendar year 1961 will average about $415 billion, compared with $404 billion in calendar year 1960.

Corporate income taxes, which have been the principal source of downward revision in receipts estimates in the past year, are estimated at $20.4 billion (net of refunds), compared with actual collections of $21.5 billion in fiscal 1960. This estimate is based on estimated before-tax profits of $45 billion in calendar 1960.

Estate and gift taxes are estimated to show a marked rise of $300 million to $1.9 billion, and excise taxes are expected to increase $200 million.

Although gross employment taxes are expected to increase substantially this year, reflecting the full-year effect of rate increases effective in January 1960, net budget receipts are not affected. Starting with this year, moreover, all receipts from the Unemployment Tax Act are being transferred to the unemployment trust fund. As a result, budget receipts are reduced by over $300 million relative to fiscal 1960. 1/

1/ Since a similar deduction is made from budget expenditures, the budget surplus is not affected.

An estimated decrease of $367 million in miscellaneous receipts is due mainly to lower deposits with the Treasury of Federal Reserve System earnings, chiefly because of a nonrecurring deposit from surplus made in 1960.

In general, receipts estimates for the current fiscal year are based on firmer estimates of the tax base and, therefore, are probably subject to considerably less revision than was the case with earlier estimates. However, two categories of receipts--the nonwithheld component of individual income taxes and estate and gift taxes--may be on the high side. Both of these revenue sources are strongly influenced by capital gains, which are very difficult to estimate. It appears that estimates of such receipts in 1961 reflect in part estimates of relatively large realized capital gains.

For the fiscal year 1961, budget expenditures are estimated as $2.4 billion higher than in the preceding fiscal year. Outlays for all major functions except interest payments on the public debt are expected to rise. The increases are attributable in varying degree to new legislation, primarily the pay raise to Federal civilian employees; to increases in relatively uncontrollable expenditures, such as grants to States for public assistance and payments for veterans' compensation, pensions, and medical care; to past commitments for such purposes as water resources projects, space exploration, and civilian aviation; and to higher Congressional appropriations for defense and other programs.

Given the typically long lag between the incurring of obligations and actual expenditures, it does not appear likely that adoption of any new programs will alter greatly the budget estimates presented in the Document. However, failure to put into effect the Budget recommendation that postal rates be increased, effective April 1, would increase the Post Office deficit by $160 million relative to Document estimates.

In the cash budget, considerable uncertainty in the Budget estimates of expenditures in the current year attaches to unemployment benefit payments. Although the Document estimate of $3.9 billion is about $1 billion higher than that presented in the Mid-year Review, it appears in light of recent trends in claims filed for compensation and of current levels of insured unemployment, that even this higher level may understate actual payments in the fiscal year by $500 million or so. Enactment of a supplemental unemployment compensation bill would also add to cash outlays in the current fiscal year. In addition, failure to put into effect the Budget recommendations that postal rates be increased, effective April 1, would increase the Post Office deficit by $160 million relative to Document estimates. A partial offset, however, may be provided by lower payments by the highway trust fund, which, on the basis of experience in the first half of the fiscal year, may aggregate slightly below Budget estimates for the year as a whole.

Estimates for Fiscal Year 1962

Document estimates of a cash surplus of $1.3 billion and in administrative budget surplus of $1.5 billion appear, at this point, unlikely to be realized. The assumptions upon which the estimates were based include a number of legislative recommendations regarding both taxes and spending which appear unlikely to be put into effect. In addition, the estimates assume a stronger recovery in economic activity than most observers consider likely at the present time.

Legislative recommendations in the Budget include proposals to increase fees and charges for Government services. Thus a recommended increase in the gasoline tax by one-half cent to 4-1/2 cents would add $810 million to budget receipts by making possible the repeal of a scheduled transfer to the highway trust fund of this amount of excise taxes as automobile parts. The recommended postal rate increase would reduce the deficit of the Post Office Department--and hence net budget expenditures--by $840 million. Altogether increases in fees and charges for Government services requested in the Budget total $1.8 billion.

Corporate profits taxes are estimated by the Budget to increase $500 million in fiscal 1962 to $20.9 billion (net of refunds). This estimate is based on the assumption that profits before tax in calendar 1961 will amount to $46 billion, compared with the estimated level of nearly $45 billion in calendar 1960. Because of the high yield per dollar from this source of revenue, it is evident that profits assumptions are critical in any receipts estimates. Thus, if profits were to average only $43 billion this year, collections in fiscal 1962 would be about $1.4 billion smaller than the Budget estimate.

In receipts estimates for both fiscal years, the Budget apparently assumes continuation of the estimated high 1959 capital gains in 1960 and 1961; this assumption is reflected in the estimated yield from estate and gift taxes as well as in nonwithheld individual income taxes. Estimates of both withheld income taxes and social security taxes are based on rising levels of wages and salaries.

Budget expenditures in fiscal 1962 are estimated at nearly $81 billion, up $2 billion from the revised estimate for fiscal 1961 and $600 million from fiscal 1959. The extent to which the new administration will recommend, and Congress pass, legislative programs which differ from those recommended in the Document cannot now be reliably estimated. Nor can it be known with reasonable certainty how much actual spending in the next fiscal year might be affected by enactment by such programs. On the assumption, however, that new programs and extensions of existing programs are limited to those which have received widest public discussion, it appears likely that administrative budget expenditures next year may exceed Document estimates by $1.5 to $2.5 billion. This estimate reflects increases for such new or expanded programs as school aid, urban renewal, aid to depressed areas, defense and foreign economic aid. Increases in cash payments could exceed this range, reflecting possible enactment of a medical care program financed by higher social Security taxes.

As a possible maximum, it is estimated that adoption of new programs, including anti-recession measures, could raise the above range of increases relative to the Document by about $3 billion. Increases of this amount might result from stepped-up spending for highway construction, housing (including urban renewal, college housing and community facilities), public works, agricultural subsidies and various social welfare programs.

FEDERAL BUDGET RECEIPTS AND EXPENDITURES, 1959-62
(Fiscal years, in billions of dollars)

Source or function	1959	1960	1961 (Estimated)	1962 (Estimated)
Total budget receipts	67.9	77.8	79.0	82.3
Individual income taxes	36.7	40.7	43.3	45.5
Corporation income taxes	17.3	21.5	20.4	20.9
Excise taxes	8.5	9.1	9.3	9.7
Employment taxes	.3	.3	--	--
Estate and gift taxes	1.3	1.6	1.9	2.0
Customs	.9	1.1	1.1	1.1
Miscellaneous receipts	3.2	4.1	3.7	3.8
Deduct: Interfund transactions	.4	.7	.7	.7
Total budget expenditures	80.3	76.5	78.9	80.9
Major national security	46.4	45.6	45.9	47.4
International affairs and finance	3.8	1.8	2.3	2.7
Commerce, housing, and space technology	3.4	2.8	3.8	3.4
Agriculture and agricultural resources	6.5	4.8	4.9	5.1
Natural resources	1.7	1.7	2.0	2.1
Labor and welfare	4.4	4.4	4.5	4.8
Veterans services and benefits	5.2	5.1	5.2	5.3
Interest	7.7	9.3	9.0	8.6
General government	1.6	1.7	2.0	2.1
Allowance for contingencies	--	--	--	.1
Deduct: Interfund transactions	.4	.7	.7	.7
Surplus (+) or deficit (-)	-12.4	+ 1.2	+ .1	+ 1.5

Closer Coordination of Monetary and Fiscal Policies

The role of monetary policy in combating recession is important but has its limitations. The supplying of bank reserves abundantly during recession contributes to declining interest rates, particularly short-term rates. But some interest rates, for example, those on home mortgages, are sluggish. Moreover, some types of borrowing do not increase much solely because of lower interest rates. Public utility borrowing is perhaps an exception to this general rule.

Fiscal policy can compensate to some extent at least for the limited effectiveness of monetary policy during a recession by doing more to restore expenditures and income. The Federal budget should be balanced, and, if possible, in surplus, over a complete business cycle, but it need not be balanced every year. In recession, planned deficits can contribute actively to recovery, in prosperity planned surpluses can counter-balance the deficits of the recession and also contribute to some reduction of the public debt.

A planned recession deficit can result from higher expenditures for unemployment compensation, for relief of depressed areas, for necessary public works and for other purposes, as well as from lower tax revenues. A planned surplus involves reduced outlays and/or higher tax revenues. The Federal tax system, being based as it is largely on income and excise taxes, does show an ebb and flow of receipts as economic conditions change. In might well, however, have even more built-in flexibility than it does over the cycle, if it is to support monetary policy more effectively. Tax revenue goes up and down a good deal but could do so even more if our tax structure were modified in a conscious effort to get greater revenue flexibility over the cycle. This would necessarily, however, be a long-range rather than an immediate objective.

January 18, 1961

Federal Reserve Transactions in U. S. Government Securities Other Than Bills in Late 1960

In late October, the System Open Market Committee authorized the manager of the System Open Market Account to purchase short-term Treasury issues other than Treasury bills in order to help supply needed reserves to the market while minimizing downward pressure on the key 3-months bill rate which threatened to fall below 2 per cent. In pursuing this policy, the manager of the System Open Market Account made outright purchases of eight short-term coupon issues totaling $315 million during three weeks in November. Of this amount, $9 million were bought from foreign and international accounts and the remaining $306 million were bought from Government Security dealers in the open market.

The longest term issue purchased was the 3-1/4 per cent note of February 15, 1962. Ninety-seven per cent of total purchases, however, consisted of certificates, notes and bonds maturing within 13 months. With the three-months bill rate fluctuating around the 2-1/4 per cent mark in late November and December, no System purchases of Governments other than bills have been made since the week ending November 23.

The System has sold short-term coupon issues during only one week--the week ending December 21, 1960. These sales totaled $202 million, of which $169 million were to the International Monetary Fund and foreign accounts, and $33 million to dealers in the open market. These latter sales were all made during one day on the basis of best price bids from dealers in a market go-around. Sales to the IMF and other foreign accounts were made in order to keep the purchases of these customers out of the market at a time when reserve factors, notably storm-induced float, were supplying large additional reserves to the banking system and putting downward pressure on bill rates. Sales of coupon issues to these accounts were accompanied by even larger sales of Treasury bills.

Outright System Open Market Operations in Securities other than Treasury Bills in 1960
(In $ million, par value)

With Government Security Dealers

Issues Bought or Sold *	4-7/8 C/I 2/15/61	4-3/8 C/I 5/15/61	3-5/8 N 5/15/61	3-1/8 C/I 8/1/61	4 N 8/1/61	2-3/4 B 9/15/61	EO 1-1/2 N 10/1/61	2-1/2 B 11/15/61	3-1/4 N 2/15/62	Total
Week Ending:										
Nov. 2	20.0	7.0			5.0	7.0		59.5		98.5
9	83.0	6.0		14.3	10.0	4.5	5.0	46.3		169.1
23	13.0	16.5		1.0		1.0			7.0	38.5
Dec. 23			- 2.0	-11.0				-11.0	-9.0	- 33.0
With Foreign and International Accounts										
Week Ending:										
Nov. 9		5.0				4.0				9.0
Dec. 21	-40.0		-40.0	-48.0				-41.0		-169.0
Gross Purchases	116.0	34.5		15.3	15.0	16.5	5.0	105.8	7.0	315.1
Gross Sales	-40.0		-42.0	-59.0				-52.0	-9.0	-202.0
Net Sales or Purchases	76.0	34.5	-42.0	-43.7	15.0	16.5	5.0	53.8	-2.0	113.1

* Includes commitments for delivery the following statement week; a minus sign denotes a sale.

March 3, 1961

Money Supply

The active money supply, as we ordinarily use the term, refers to the supply of means of payment in the hands of the public (that is, demand deposits other than interbank and U. S. Government less cash items in process of collection plus currency outside banks). In the October 1960 Federal Reserve Bulletin, the System inaugurated a new statistical series for measuring the money supply. In addition to incorporating certain conceptual improvements, such as broadening the concept of money to include demand deposits of mutual savings and foreign banks in U. S. commercial banks and deducting Federal Reserve float, the major advantages of the new series are that it is based on averages of daily figures rather than on figures for a single date and appears semimonthly rather than only monthly, as is the case with the end-of-month series. Seasonally adjusted estimates for each semimonthly period, together with various components on an unadjusted basis, are released to the public generally about 10 days after the close of each semimonthly period.

After declining \$3.9 billion from the postwar peak in July 1959 to June 1960, the seasonally adjusted money supply advanced \$1.9 billion through the first half of February 1961. This increase, however, was small compared to the record expansion in commercial bank loans and investments that has occurred since June 1960 in response to substantial easing in monetary policy. The principal counterpart to that expansion was a record \$5.5 billion rise in commercial bank time deposits, seasonally adjusted, from June 1960 through January 1961.

Growth in money supply from June through mid-February was at an annual rate of about 2 per cent. In the comparable periods of the 1957-58 and the 1953-54 downturns, money supply showed little change. Time deposits at commercial banks also have expanded at a more rapid pace in the current downturn than in the two previous ones.

Money Supply

Seasonally Adjusted
(Billions of dollars)

	Total	Demand deposit component	Currency component
MONTHLY			
1950--December	115.3	90.3	25.0
1957--December	135.5	107.2	28.3
1958--December	140.8	112.2	28.6
1959--July (postwar high)	143.3	114.3	29.0
December	141.5	112.6	28.9
1960--January	141.3	112.3	29.0
February	141.0	112.1	29.0
March	141.6	111.6	29.0
April	140.5	111.4	29.1
May	139.9	110.9	29.0
June	139.4	110.5	28.9
July	139.6	110.7	28.9
August	139.7	110.8	28.9
September	140.4	111.5	29.0
October	140.6	111.6	29.0
November	140.2	111.2	29.0
December	140.4	111.4	29.0
1961--January p	140.6	111.7	28.9
SEMIMONTHLY			
1960--December (1)	140.3	111.4	28.9
(2)	140.5	111.5	29.0
1961--January (1)	140.2	111.3	28.9
(2)	141.0	112.0	29.0
February (1) p	141.3	112.4	28.9

p - Preliminary.

Misc.

Author: George Shea

Article Title: The Outlook Appraisal of Current Trends In Business and Finance

Journal Title: Wall Street Journal

Date: March 20, 1961

Author: Felix Belair Jr.

Article Title: Reserve Official Disputes Kennedy on Jobless Cause: Martin Asserts 'Hard Core' Unemployment Is Heavy Even During Prosperity: Hits Spending as Cure: Dillon Forecasts Upturn but Sees a Budget Deficit as Unavoidable This Year

Journal Title: New York Times

Date: March 8, 1961

April 21, 1961.

Mr. W. Braddock Hickman,
Senior Vice President,
Federal Reserve Bank of Cleveland,
Cleveland 1, Ohio.

Dear Mr. Hickman:

As Mr. Martin will be away from the office, on an official trip abroad, for about a month, I wanted to acknowledge receipt of your note to him of April 19. I know that he will appreciate your nice comments on his return.

Sincerely yours,

(Miss) Margaret Muehlhaus,
Secretary to Mr. Martin.

FEDERAL RESERVE BANK

OF CLEVELAND

OFFICE OF
SENIOR VICE PRESIDENT

April 19, 1961

Mr. William McChesney Martin, Jr.
Chairman, Board of Governors of the
Federal Reserve System
Washington 25, D. C.

Dear Bill:

This is a delayed reaction to your statement of March 7 before the Joint Economic Committee, which I have had occasion to refer to again and again. It is by far the clearest and most concise statement that I have seen of the Federal Reserve's recent operations, problems, and attitudes. You have told me of your concern about the problem of communicating the System's position to outsiders, which I share. In my opinion, this is the way to do it, and I hope we will have more of the same.

Congratulations and best wishes.

Sincerely,

Brad

W. Braddock Hickman

April 10, 1961

To Board of Governors Subject: Testimony of Council

From Jerome W. Shay of Economic Advisers

This morning the Council of Economic Advisers concluded their testimony before the Joint Economic Committee. Caution and restraint accompanied most, if not all, of their testimony.

There was a good deal of discussion concerning the need for lower interest rates to help get the economy going again. The Council seemed to agree that the sluggishness in the movement of interest rates is attributable mainly to the balance-of-payments problem, which has operated to restrain monetary policy. It was pointed out that but for the balance-of-payments problem the discount rate could have been lowered and operations of the Federal Reserve would have been such as to have resulted in much lower short-term interest rates with the resulting downward pressure on long-term rates. After reference to the action announced on February 20 by the Open Market Committee, hope was expressed that lower rates for long-term securities will occur, without which the Council felt that recovery could not be attained.

Senator Douglas asked Mr. Tobin if he aggreed with his (Douglas') position, namely, that the Federal Reserve should operate to expand the money supply by three per cent a year and do so through open market operations in long-term securities, scrapping the "bills only" policy and discontinuing reductions in reserve requirements. Mr. Tobin replied that he did not wish to approve any specific rate for increasing the money supply and that it is his belief that the Federal Reserve should have available for its use all of its instruments of credit control, although Mr. Tobin indicated he feels that dealing in the long-term market is desirable at this time, because of the restraints resulting from the international balance-of-payments problem. In this connection, Mr. Tobin observed that one of the problems with current operations of the Federal Reserve is whether funds will merely move from the long end to the short end of the market and an answer to this, he felt, will depend upon further experimentation.

When Senator Douglas, in effect, gave Mr. Tobin an opportunity to indicate that the Federal Reserve should have moved into the longer terms before February 20, Mr. Tobin replied that the Federal Reserve had made moves in that direction before the February 20 announcement.

One of Mr. Heller's responses seemed to indicate that the balance-of-payments problem is such now as not to operate as a restraint on monetary policy. On the other hand, however, most of the emphasis was on the need for lower long-term rates, and there was no suggestion that monetary policy should relax or revert to any former posture.

There was virtually no reference to the alleged "conflict" between Chairman Martin and Mr. Heller with respect to structural unemployment, et cetera, although Senator Proxmire did make reference to his thought that Chairman Martin had taken a less "expansionary" view than had the Council.

Mr. Heller, in effect, reaffirmed that both fiscal and monetary policy should play a part in increasing the growth rate and reducing unemployment but that a total package of remedies, some available and some proposed, would be necessary, and, in his judgment, the unemployment problem will continue as a very "tough" one.

The Council appeared this morning without a formal statement, although there was submitted to the Committee written replies to certain questions that had been submitted by Congressman Curtis. Quoted below is Congressman Curtis' question 14, followed by the Council's reply:

"Question 14: 'The Chairman of the Federal Reserve Board testified before the JEC and he gave a picture of the economics behind the relatively high incidence of unemployment that many people, including myself, thought was at variance with the one expressed in your testimony. Since then, Mr. Martin has submitted a further statement made after he had a chance of reviewing yours. He states, "It seems to me that the apparent differences with my testimony (and yours) are mainly ones of definition and emphasis." With this I agree and I think, far from reconciling the differences, Mr. Martin's further statement confirms the differences in both emphasis and definition to be fundamental differences. Your statement is very postive. On page 15 you state, "Some have attributed the growth of unemployment in recent years to changing characteristics of the labor force rather than to deficiencies in total demand...Expansion of overall demand, it is argued, will not meet this problem; it can only be met by educating, restraining, and relocating unsuccessful job-seekers.

'"The facts clearly refute this explanation of the rise of unemployment over the last 8 years."

'We are primarily interested in examining into the problems of unemployment so that we can apply the proper remedies. Your analysis suggests expanding overall demand (which I believe you regard as being synonymous with disposable income, which I do not). Mr. Martin clearly does not recognize this as a method of attacking structural unemployment.

'I would be pleased to have your comments.'

"Our statement and our calculations demonstrated that recent <u>increases</u> in the unemployment rate at cyclical peaks could not correctly be attributed to <u>increases</u> in the extent of structural unemployment. We know of no evidence that contradicts this conclusion and the analysis that supports it.

"The Council's statement recognized the importance of structural unemployment. We stated (as did Chairman Martin) that policy should move ahead simultaneously against structural unemployment and against unemployment stemming from weak aggregate demand. We pointed out (as did Chairman Martin) that expansionary fiscal and monetary policy would create an environment in which the pull of jobs in the growing sectors of the economy would attract workers from the declining sectors and areas. Thus, general prosperity contributes to the effectiveness of policies aimed specifically at structural unemployment. Our March 6th statement said:

> "' Measures to improve the mobility of labor to jobs and jobs to labor, to better our educational facilities, to match future supplies of different skills and occupations to the probable pattern of future demands, and to improve the health of the population--these are and should be high on the agenda of national policy. But they are no substitute for fiscal, monetary and credit policies for economic recovery. Adjustments that now seem difficult, and unemployment pockets that now seem intractable, will turn out to be manageable in an environment of full prosperity.'

"The 4 percent unemployment rate we mentioned as a clearly attainable target allows plenty of room for the unemployment stemming from shifting demands and technical progress. The unemployment rate is close to 7 percent now. As recently as February 1960 it was 4.8 percent. A rise in the unemployment rate by 2 percent of the labor force in the short space of a year can scarcely be attributed to basic changes in the structure of the economy and of the labor force. It is the result of the recession, i.e., of weakness in overall demand. Nor can all of the 5 percent unemployment of early 1960 be accepted as hard-core structural unemployment; there is independent evidence that the economy was then operating short of reasonable capacity.

"We certainly do not view 4 percent unemployment as a rock-bottom minimum. As policies to improve the mobility and the skill composition of the labor force take effect, it will be possible in sustained prosperity to hold the rate of unemployment somewhere below that figure.

"Finally, we do not regard <u>overall demand</u> as synonymous with <u>disposable income</u>. <u>Overall demand</u> is the aggregate of spending by government, business, and households. Consumer spending, which is related to <u>disposable income</u> in the manner explained in #4, is only one component, though the single largest component, of overall demand."

cc: Each Board Member
Messrs. Thomas, Young, Molony, Fauver, Knipe, Ford, Alderfer, Sherman, and Noyes

Chairman Martin.

March 31, 1961.

To Board of Governors Subject: Joint Economic Committee Hearing

From Jerome W. Shay

The Joint Economic Committee has scheduled a hearing for Monday, April 10, to hear again from the Council of Economic Advisers. It may be recalled that when Messrs. Heller, Tobin and Gordon appeared before the Committee on March 6 it was then arranged that they would come back at a future date for further questioning. It will be recalled also that at the President's Press Conference at which the alleged disagreement between Mr. Martin and Mr. Heller regarding structural unemployment was referred to the President said that he understood that the Committee was going to have both Mr. Martin and Mr. Heller back for further testimony.

The information above concerning the scheduled hearing for April 10 indicates that nothing more is intended than the Committee's original idea to have a return engagement with just the Council of Economic Advisers.

cc: Each Board Member
Messrs. Thomas, Young, Molony, Fauver, Knipe, Ford, Alderfer, Sherman, Noyes, and Marget.

Chairman Martin

March 27, 1961

To Board of Governors

From Jerome W. Shay

Subject: Testimony of Budget Director Bell before Joint Economic Committee

This morning, David Bell, Director, Bureau of the Budget testified before the Joint Economic Committee.

With respect to the budget for fiscal 1961, Mr. Bell indicated a deficit of about $2.2 billion. He said that all figures for fiscal year 1962 are tentative, since military phases of the budget still are in process of preparation. Thus there has been no change in the situation since the President's budget message of March 24.

There was no specific reference to the Federal Reserve during Mr. Bell's testimony.

With respect to the state of the economy, Mr. Bell said that we are just about at the turning point, so that during the summer and fall of this year we will be moving ahead at a "pretty good rate". Nevertheless, it was his view that by the end of this year we still would have about six or six plus per cent unemployment. He said that the unemployment problem is not just a short-run-recession problem, since, in addition to the cyclical phase of unemployment, there is the long-run problem--the problem of "long-term slack" in employment. The latter aspect of the problem, he indicated would have to be met with special measures, such as programs to retrain persons displaced by automation.

Mr. Bell said he does not expect unemployment to get as low as four per cent very soon, since to pursue policies that would bring about a reduction to that figure would be risking serious inflation.

According to Mr. Bell, the President's judgment so far is that the plans thus far announced to deal with the economy are adequate, although renewed looks at the over-all economy will be taken from time to time. On the basis of this, Mr. Bell indicated that there is no indication of a tax cut.

While a strong majority of the Committee members put in an appearance at the hearing this morning, very few stayed to question Mr. Bell to any significant extent.

cc: Each Board Member
Messrs. Thomas, Young, Molony, Fauver, Knipe, Ford, Alderfer, Sherman, and Noyes

March 28, 1961.

Dear Dave:

Thank you for sending me a copy of your testimony on the budget, which I will study with great interest.

I know you are glad to have this over with for the moment.

My best, as always.

Cordially yours,

Wm. McC. Martin, Jr.

The Honorable David E. Bell,
Director,
Bureau of the Budget,
Washington 25, D.C.

EXECUTIVE OFFICE OF THE PRESIDENT
BUREAU OF THE BUDGET
WASHINGTON 25, D. C.

March 27, 1961

Dear Bill:

I thought you might like to have a copy of the testimony on the budget which I gave before the Joint Economic Committee earlier today.

With best regards.

Sincerely yours,

Dave

Director

Honorable William McC. Martin
Chairman, Board of Governors of the
Federal Reserve System
Federal Reserve Building
Washington 25, D. C.

Enclosure

EXECUTIVE OFFICE OF THE PRESIDENT
BUREAU OF THE BUDGET
Washington 25, D. C.

FOR RELEASE ON DELIVERY
Expected at 10:00 a.m.
Monday, March 27, 1961

STATEMENT OF DAVID E. BELL,
DIRECTOR OF THE BUREAU OF THE BUDGET,
BEFORE THE JOINT ECONOMIC COMMITTEE

Mr. Chairman and Members of the Committee:

It is a pleasure to appear before you today to discuss with you the current budget outlook as presented in the President's message of March 24. The figures that I am presenting today reflect the administrative actions and recommendations to the Congress which have resulted from the President's review, over the past two months, of the programs and activities of the agencies of Government. This review is complete except for the defense program, on which the President will transmit his recommendations shortly.

Additional budgetary details supporting the figures in this statement are shown in a supplementary paper which is attached.

THE CURRENT BUDGET OUTLOOK

A. Fiscal Year 1961

In the budget which was sent to the Congress on January 16, 1961, the previously estimated surplus had almost disappeared. In January, 1960, the budget for fiscal 1961 anticipated continued and vigorous economic expansion and showed a surplus of $4.2 billion. In early October, in the midyear budget review, with signs of a sagging economy evident, the estimated surplus had shrunk to $1.1 billion. In January, 1961, expenditures in the current fiscal year were estimated at $78.9 billion and revenues at $79.0 billion, yielding a surplus of less than $0.1 billion. This estimated surplus depended upon a number of assumptions with respect to both revenues and expenditures that now seem to have been in error.

Expenditures of the Department of Defense were clearly underestimated. Excluding the effects of any program changes made by the present administration, these expenditures in fiscal 1961, including military assistance, are now estimated to exceed the official estimate made last January by $544 million.

The January budget also assumed that the Congress would enact postal rate increases effective April 1, 1961, in time to decrease budget expenditures for the postal service by $160 million this year. It is now obvious that any increases in postal rates are unlikely to take effect before July 1. In several other instances, the January estimates of 1961 expenditures were understated, such as $50 million for loans of the Export-Import Bank and $74 million for veterans direct housing loans. On the other hand, expenditures were overestimated in some cases, notably by $423 million for farm price supports and related activities.

The net upward revision which it is necessary to make in the 1961 expenditure estimate, for the program set forth in the January budget, will amount to approximately $384 million.

Revenue prospects are difficult to assess at this time, since much depends on the seasonally heavy tax collections in March and April. However, the best judgment of the Treasury Department is that budget receipts in fiscal 1961 may fall short of the January budget estimate by as much as $500 million, principally because of a shortfall in individual income tax and excise tax collections.

Thus, excluding the effects of any proposed programs or budget amendments by this administration, we would have a 1961 deficit of about $800 million rather than the thin surplus of $79 million that was estimated in January.

Certain of the recommendations that the President has made to the Congress, and administrative actions that he has directed, will add to expenditures in this fiscal year. These increases are estimated at about $1.4 billion. This amount includes $574 million for temporary extended unemployment benefits (including railroad unemployment), $256 million for military functions of the Department of Defense (including speedier contract payments, acceleration of Polaris, and airlift modernization), $225 million for the price support and related activities of the Commodity Credit Corporation, $118 million for domestic surplus food distribution, and $64 million for farm ownership, operating, and housing loans. In total, therefore, the current prospect for fiscal 1961 is for budget expenditures of $80.7 billion, receipts of $78.5 billion, and a deficit of about $2.2 billion.

TABLE 1. ESTIMATED BUDGET TOTALS, FISCAL 1961

(In millions)

	Receipts	Expenditures	Surplus (+) or Deficit (-)
January 16, 1961 budget totals	$79,024	$78,945	$ +79
Administrative actions and recommended program changes	--	1,364	-1,364
Total	79,024	80,309	-1,285
Necessary revisions in estimate for January budget program (not related to new proposals)	-500	384	-884
Revised estimate, budget totals	78,524	80,693	-2,169

B. Fiscal Year 1962

In the January budget, expenditures of $80.9 billion were proposed for fiscal 1962 and revenues were estimated at $82.3 billion, yielding a budget surplus of $1.5 billion. The estimate of revenues assumed a prompt and brisk upturn in economic activity, as well as the enactment of various legislative proposals to increase revenues over their yield under existing laws.

As the President stated last week in his message on budget and fiscal policy, his recommendations for new programs and for appropriation amendments, excluding defense, will increase expenditures in fiscal 1962 by about $2.3 billion.

The additional nondefense expenditures include:

. . . . $500 million for aid to elementary and secondary schools, for the States and local school districts to use as they determine for construction, teachers salaries, and special projects; an additional $30 million is estimated to be spent in 1962 for higher education ($21 million) and for medical education ($9 million).

. . . . $478 million for the Department of Agriculture, including $164 million for the costs of the Commodity Credit Corporation in supporting farm prices, distributing surplus foods abroad, and other activities, $169 million for domestic distribution of surplus foods, the food stamp pilot program, and the school lunch and special milk programs, $122 million for farm ownership, operating, and housing loans, and smaller amounts for the Forest Service and the Rural Electrification Administration.

. . . . $440 million for the fiscal 1962 portion of the temporary extended unemployment compensation program. Under this program, as recommended by the President and passed by the Congress, the duration of benefits will be extended up to 13 weeks for unemployed workers who exhaust their benefits under regular programs. These extended payments will be financed through advances from the general budget to the trust fund. They will be repaid later from the proceeds of the temporarily increased Federal unemployment tax.

. . . . $215 million for aid to the dependent children of the unemployed -- to help relieve distress and prevent the enforced breaking-up of families.

. . . . $214 million for the Housing and Home Finance Agency, covering the cost of the programs advanced by the President for low-cost housing, urban renewal, college housing loans, public facility loans, and housing for the elderly.

. . . . $95 million for veterans benefits, consisting of $65 million for the selective cost-of-living increases and adjustments in compensation payments to service-disabled veterans proposed by the President and $30 million for direct housing loans.

The proposed increases in expenditures can be expected to generate an increase in economic activity and in incomes over the next year, which will, in turn, yield an increase in tax revenues, estimated in the President's message at $900 million.

Thus, the $2.3 billion increase in 1962 expenditures proposed by the President is less than the originally estimated surplus of $1.5 billion plus revenue increases of $900 million from the accelerated economic recovery that the President's program could be expected to generate. The new budgetary proposals for 1962 have, of course, as stated in the President's State of the Union message, been kept within this limit intentionally. Of themselves, except for the additional defense needs, they would not unbalance the budget submitted to the Congress by the preceding administration.

However, it is now apparent that both the expenditure and revenue estimates in the January budget were in error.

The January budget estimate of expenditures for farm price supports and other activities of the Commodity Credit Corporation was based on assumptions as to output, domestic consumption, and exports of farm commodities which now appear to be optimistic. On this count alone, $249 million needs to be added to the earlier estimate. Interest on the public debt, considering only the program set forth in the January budget but allowing for the presently expected shortfall in revenues, is now estimated to rise by about $100 million over the January figure. Taking account of a number of other increases and decreases in expenditure estimates, the total net effect of reestimating the January program is to increase the 1962 expenditure estimate by $372 million.

Federal revenues in fiscal 1962 will depend largely on the course of the economy during the calendar year 1961. The Treasury and the Council of Economic Advisers now tell us that the economic assumptions underlying the budget sent to the Congress in January would have been unrealistically optimistic if the Government program advanced in that budget has been adopted. In fact, if the budget expenditure program recommended in January had prevailed, a revenue estimate of $80.5 billion for fiscal 1962 would have been closer to the mark than the $82.3 billion predicated

Allowing for the improvement in economic activity that the present budget proposals would generate, budget receipts for fiscal 1962 are now estimated at $81.4 billion. While corporation income taxes are not expected to fall significantly below the January estimate, individual income taxes and excise taxes are now expected to be substantially lower.

The present estimate of $81.4 billion of budget receipts for 1962 assumes the extension of corporate income and excise tax rates and the adoption of the President's proposal to prevent the diversion of taxes from the general fund to the highway trust fund.

All the revisions in the January budget estimates for 1962, except for the defense program, are summarized in Table 2. As that table clearly shows, a budget deficit is now in prospect for 1962, and that deficit will be the consequence of the overestimation of revenues and underestimation of expenditures in the January budget.

TABLE 2. ESTIMATED BUDGET TOTALS, FISCAL 1962

(In millions)

	Receipts	Expenditures	Surplus (+) or deficit (-)
January 16, 1961 budget totals.....	$82,333	$80,865	$1,468
Recommended program changes, except defense, and added revenue from increased economic activity generated by new proposals..........................	900	2,322	-1,422
Total....................	83,233	83,187	+46
Necessary revisions in estimate for January budget program (not related to new proposals)........	-1,800	+372	-2,172
Revised estimate, budget totals....	81,433	83,559	-2,126

Note: If the Congress adopts the President's proposal for a revolving fund for foreign aid loans, total loan disbursements will not change but the recorded totals of budget receipts and expenditures in 1962 would each be reduced by about $300 million.

RECOMMENDED REVISIONS IN TRUST FUND PROGRAMS

A number of the programs recommended in the President's messages would be financed through trust funds, outside of the regular budget. They include mainly (1) improvements in the existing system of old-age, survivors, and disability insurance, (2) provision of medical care for the aged on a self-financed basis through the old-age, survivors, and disability insurance system, (3) a speedup in the payment of veterans life insurance dividends, and (4) increased funds for the Federal-aid highway program.

Table 3 sets forth the revisions in the estimates of trust fund receipts and expenditures.

The effect of the temporary extended unemployment compensation program on the budget has already been mentioned. Advances from the general budget to the trust fund and trust fund payments are shown in Table 3. However, pending the determination of firm proposals for strengthening the permanent Federal-State unemployment insurance system, no estimates have been included for the revision of the permanent program.

The revisions recommended by the President for old-age, survivors, and disability insurance benefits will add $1.1 billion to trust fund expenditures in fiscal year 1962. To finance these increased payments, tax increases of one-quarter of one percent each on employers and employees are to go into effect on January 1, 1963. The inclusion of medical care for the aged in the social security system will not affect trust fund expenditures until fiscal year 1963. The proposed increase in the covered wage base from $4,800 to $5,000 would be effective January 1, 1962, and would affect trust fund revenues only slightly in fiscal 1962; a further tax rate increase of one-quarter of one percent on employers and workers would go into effect on January 1, 1963.

As a result of the early payment of dividends under the veterans life insurance system, trust fund expenditures of $105 million will be shifted from fiscal year 1962 into fiscal 1961.

The entire balance of Federal-aid highway funds scheduled for this fiscal year has been made available to the States. Efforts are underway to obtain the cooperation of the States in effecting a speedup to get highway projects under construction more rapidly, but no change has been made in the January estimate of highway trust fund payments for 1961. A proposed expansion of the presently authorized Federal-aid highway program, together with the necessary increase in taxes to support it, was transmitted to the Congress earlier this month. If the increases recommended are promptly enacted, further acceleration of highway construction will result in increased trust fund payments in 1962 of $60 million and increased receipts of $15 million.

A much larger than expected volume of mortgage sales early this calendar year has reduced by $731 million the net expenditures for 1961 estimated in January for the secondary market operations of the Federal National Mortgage Association. No further substantial sales are anticipated under present policies, however, and the secondary market operations are being used to support a reduction in the interest rate from 5-3/4 percent to 5-1/2 percent on loans insured by the Federal Housing Administration.

TABLE 3. ESTIMATED TRUST FUND EXPENDITURES AND RECEIPTS

(Fiscal years. In millions)

	Expenditures		Receipts	
	1961	1962	1961	1962
January 16, 1961 budget program	$24,102	$25,155	$24,239	$25,189
Administrative actions and recommended program changes:				
Old-age, survivors, and disability insurance:				
Liberalization	55	1,105	--	a/ -21
Medical care	--	--	--	40
Unemployment trust fund:				
Temporary unemployment compensation and employment service expansion	509	453	564	446
Extension of railroad unemployment benefits	8	15	24	--
Veterans life insurance:				
Accelerated dividend payments	105	-105	a/ -1	--
Federal-aid highways	--	60	--	15
Federal National Mortgage Association purchases (net)	200	--	--	--
Total program changes	877	1,528	587	480
Necessary revisions in estimate for January 16, 1961 budget program (not related to new proposals):				
Unemployment trust fund	300	--	--	--
Federal National Mortgage Association purchases (net)	-731	--	--	--
Revised estimate, trust fund totals	24,548	26,683	24,826	25,669

a/ Reduced interest receipts.

RECEIPTS FROM AND PAYMENTS TO THE PUBLIC

Because trust fund and certain other transactions are not included in the budget totals, and because the budget and trust fund totals include several billions of dollars of intragovernmental transactions, a consolidation of all accounts--excluding intragovernmental receipts and payments--is necessary to show the flow of money between the Federal Government and the public. A summary derivation of these consolidated cash totals is shown in Table 4.

TABLE 4. ESTIMATED RECEIPTS FROM AND PAYMENTS TO THE PUBLIC

(Fiscal years. In millions)

Description	1961 January estimate	1961 Current estimate	1962 January estimate	1962 Current estimate
Receipts from the public:				
Budget receipts........................	$79,024	$78,524	$82,333	$81,433
Trust fund receipts....................	24,239	24,826	25,189	25,669
Deduct:				
Intragovernmental transactions........	4,195	4,783	4,294	4,719
Seigniorage on silver..................	63	63	82	82
Total..............................	99,005	98,504	103,145	102,301
Payments to the public:				
Budget expenditures....................	78,945	80,693	80,865	83,559
Trust fund expenditures................	24,102	24,548	25,155	26,683
Government-sponsored enterprise expenditures (net)....................	-196	-196	421	421
Deduct:				
Intragovernmental transactions........	4,195	4,783	4,294	4,719
Excess of interest accruals over payments, etc.	725	725	314	314
Total..............................	97,931	99,537	101,832	105,630
Excess of receipts over payments (+) or payments over receipts (-)..............	+1,074	-1,033	+1,313	-3,329

NOTE: Detail may not add to totals because of rounding.

FISCAL POLICY: THE LONG RUN

In this first appearance before the Joint Economic Committee, I should like to say a few words about the basic approach of the new administration to fiscal policy.

First, let me say something about the long-run trend in Federal receipts and expenditures. This is a growing country with an expanding labor force, continually better technology, and a steadily increasing capacity to produce. In these circumstances, as the President said in his budget and fiscal policy message, "Federal revenue and expenditure levels must be adequate to meet effectively and efficiently those essential needs of the Nation which require public support as well as, or in place of private effort." The United States has very large resources to meet its obligations of world leadership and, at the same time, to achieve major advances in well-being at home. The question at any given time, within the total of the Nation's capacity, is one of judgment as to the relative importance of the various alternative public and private uses of resources.

At the present time, the President has proposed that we should move ahead along certain lines -- to improve the education, health, and welfare of our people, to conserve and develop our natural resources, to provide needed public facilities, to increase scientific research and promote technological progress, and to strengthen free world defenses. It would be a serious error of public policy, as well as false economy, to reject these public programs on an arbitrary assumption that "we cannot afford them." This Nation can afford higher expenditures, public or private, up to the limit of its capacity to produce -- a limit it has not approached for several years. The question is one of relative importance. Each expenditure must be evaluated, in the President's words, "in terms of our national needs and priorities . . . and compared with the urgency of other budgetary requirements." The relevant criterion in determining the desirability of a proposed use of resources for a public purpose is its value to the country in comparison to the value of using the same resources for other purposes, public or private.

Meeting our national needs responsibly in the years ahead may well mean increased rather than reduced Federal spending, until and unless we can arrive at a satisfactory agreement for the reduction of world armaments. As a matter of fact, budget studies published by the preceding administration, to which the President referred in his budget message, indicate that under its policies, and under existing laws and programs, annual Federal budget expenditures would be likely to increase by $15 to $20 billion in the coming decade, and annual trust fund outlays by another $10 to $15 billion.

By far the largest proportion of Federal Government purchases of goods and services is for national security purposes. The future level of expenditures for national security will depend in large part upon world events in relation to United States interests, commitments, and risks. If there is no worsening of international tensions, and if changes in military technology continue along the lines that seem quite possible, the increase in defense expenditures in the years ahead might be moderate, and the percentage of the gross national product needed for defense purposes might decline, as it has in the past few years. It is also quite possible, of course, that world tensions may increase, or technological changes of a different type may come along, which would require a larger share of the national product for defense purposes.

If it proves possible to meet national security needs with a declining share of the national product, the needs of the Nation for education, health, community development, scientific research, development of natural resources, and other programs might be met without an increase, and perhaps with a decrease in the share of the Nation's growing output of goods and services used by the Federal Government.

On the other hand, Federal transfer payments (such as social security benefits and other Federal programs that do not involve a Government claim on the Nation's current output of goods and services) and grants to States will probably continue to grow, and perhaps also rise as a proportion of the gross national product. These disbursements as well as direct purchases of goods and services will have to be taken into account in determining the Government's total revenue needs.

As stated in the President's economic message of February 2, the American economy was capable in calendar 1960 of an output of $535 billion, 6 percent above the $503.5 billion actually produced. Moreover, our economic potential now grows at a rate of at least 3.5 percent per year. At this rate, the gross national product would increase to more than $750 billion by 1970 in present prices. At today's tax rates, this growth would yield an increase in budget revenues from $77.8 billion in fiscal 1960 to approximately $120 billion in fiscal 1970. These are minimum estimates. With proper public and private policies, we should be able to achieve a significantly higher rate of growth in national output.

The President's economic and fiscal recommendations have been prepared with this objective in mind. The expenditures proposed are an important part of a national effort to close the gap between our actual and our potential output and to achieve adequate economic growth. This is particularly true of capital expenditures of Government that are needed to reinforce private capital expenditures, and expenditures to improve the quality and productivity of our human resources. These expenditures are as essential to economic growth as are private investment outlays.

FISCAL POLICY: THE SHORT RUN

Within the framework of long-run goals, fiscal policy should be adapted to the needs of the current economic situation. "Federal expenditure and revenue programs," to use the President's words, "should contribute to economic growth and maximum employment within a setting of reasonable price stability." Moreover, as the President noted, because of the limits which the current balance of payments deficit places on the exercise of monetary policy, fiscal policy must assume a heavier burden of responsibility for economic stability and growth.

Certain Federal expenditures automatically exercise a contracyclical influence. Unemployment compensation benefits, and old-age and survivors insurance payments (reflected mainly in trust fund accounts rather than in the regular budget), for example, tend automatically to rise in times of economic decline and to fall, or in the case of OASI benefits to rise less rapidly, in times of boom.

Most Federal expenditures, however, exhibit no such automatic, contracyclical pattern, and it is necessary to make judgments as to their magnitude and timing in relation to the current economic outlook. Federal programs differ greatly, of course, in the degree to which they can or should be altered in response to fluctuations in business activity. Defense expenditures, to take a major example, should be set at the level needed, no more and no less, to provide adequately for the defense of this Nation. Their timing can sometimes be adjusted, within limits, for economic reasons, but their magnitude should be determined by defense needs. The same is true of expenditures to enact and enforce legislation, to assure justice, to protect our people against crime and internal violence, to represent the interests of citizens of this country in countries abroad, and to provide numerous other services of Government.

At the same time, there are activities of Government which may or may not be worth undertaking, depending on the extent to which the Nation's resources are being utilized. If private demands are high, and productive resources are being pushed to capacity operations with consequent upward price pressures, then Government should retrench. Less urgent projects should be deferred. On the other hand, when private demands are slack, and productive resources are idle, such deferred public projects should be undertaken and can help economic recovery while filling a specific public need. Moreover, public works projects -- especially those with a fairly short completion time -- can be accelerated in times of low employment and retarded in times of high employment. The procurement of certain supplies and equipment can be speeded up when private spending is declining and slowed down when private spending is rising without significantly affecting the efficiency of the Government's inventory and supply systems. It was for this purpose that the President directed, a few weeks ago, a speedup in construction and procurement already funded.

Federal expenditure programs can be increased or decreased for the purpose of offsetting business cycle movements, however, only within limits. Public expenditure programs typically cannot be turned on and off like a faucet. The authorization and appropriation processes are inevitably time-consuming. Engineering, planning, and procurement arrangements also take time. This problem of an inevitable timelag is less serious now, when there is persistent slack in our economy, than it would be in more favorable circumstances. Programs of intrinsic merit can be initiated now without fear that their impact will be felt too late, when it is not needed. But steps to speed up public expenditure programs must always be taken with due care, lest waste and inefficiency result.

On the revenue side of the budget, tax collections, even with no change in tax rates, respond fairly promptly and more than proportionately to fluctuations in the general level of employment and incomes. Although this sensitivity to the business cycle is probably a reflection of other tax objectives rather than of conscious design, it is nevertheless desirable. We have learned from long experience that an attempt exactly to match tax revenues to expenditures each year, regardless of the level of business activity, would be not only extremely difficult, but would be positively harmful.

A decline in revenues relative to expenditures in times of falling economic activity means that the Federal Government is contributing to recovery by reducing the net amount of purchasing power that it is siphoning out of the private income stream. Thus consumers and businesses have more funds to spend than they would otherwise have. Conversely, in times of boom and inflationary pressures arising from excess private demand, a rise in Federal revenues has the opposite effect; it siphons some of the excess purchasing power out of the private income stream. In these ways, the automatic response of tax revenues to economic activity contributes to economic stability.

The sensitivity of Federal revenues and payments to overall economic conditions helps to give the economy a "built-in" stability, valuable in arresting recessions and checking inflationary booms. But "built-in" stabilizers can at best do only part of the job. The automatic response of the tax system restores a fraction, but only a fraction, of the loss of income and demand in recession. Similarly, it can do no more than offset part of the increases in spending in an inflationary period.

The automatic stabilizers leave plenty of room for discretionary policies of economic stabilization, both fiscal and monetary. A major surge in private spending -- such as that which occurred shortly after the outbreak of the Korean War -- calls for an increase in tax rates; and indeed the Congress then acted promptly and wisely to provide such an increase. Conversely, a serious or prolonged decline in economic activity relative to the Nation's potential would call for a reduction in tax rates.

As the Chairman of the Council of Economic Advisers emphasized in his testimony before this Committee, we must be alert not to permit tax and expenditure policies to stabilize employment and production at levels far short of full capacity. As the capacity of the economy grows, potential revenues grow even faster. A tax and expenditure structure that yields a deficit in a given year could well yield a surplus several years later when, even though the rate of unemployment is the same, the output of the economy is larger. Tax and expenditure programs should be adjusted from time to time to assure that automatic surpluses do not develop under circumstances when they would be harmful. When the economy is operating at its full potential, and when investment funds are in short supply, a surplus contributes to economic growth by permitting some retirement of public debt, thus releasing savings for needed investment in private plant and equipment. But a surplus while unemployment is high, resulting from deliberate action or simply from the automatic response of the tax structure to growth in the Nation's productive potential, can of itself prevent the attainment of full employment. Under such circumstances, a budget deficit is clearly essential to economic recovery.

THE BUDGET AND THE BALANCE OF PAYMENTS

The magnitudes of our Government expenditures abroad are substantial. The President has directed that a close review of all governmental activities be made in order to economize on the use of dollars abroad. But with the best efforts to economize, we can anticipate that our total foreign expenditures will remain large until major disarmament becomes possible.

It would be a serious error to eliminate essential expenditures solely for foreign exchange reasons. As stated in the President's message on balance of payments and gold, we must not try to strengthen our balance of payments at the cost of either military operations abroad that are required for the safety of our people, or of economic progress in the less developed countries. There are other and better ways of ensuring a reasonable balance in our basic economic relationships with foreign countries.

It is not easy to assess the impact of Federal expenditures on the U. S. balance of payments. For one thing, expenditures for foreign goods and services have taken place within total agency programs and, with few exceptions, have not been shown separately in the budget. Now that the need for estimates of foreign exchange expenditures is more apparent, the Treasury and the Budget Bureau are taking steps to identify direct outlays for foreign goods and services, and as the President directed in his Balance of Payments message, these will be considered in making budgetary decisions. There is, however, a deeper problem. The impact of Federal outlays on the Nation's balance of payments is not measured by the direct costs of foreign purchases. There is the additional question of what happens to the dollars spent abroad. A direct outlay for a foreign purchase which results in an immediate offsetting purchase of American products has, of course, no net effect whatever on the balance of payments. It is necessary therefore to be very careful in judging the relationships between the budget and the balance of international payments.

EFFICIENCY AND ECONOMY IN GOVERNMENT SPENDING

It is an essential element of fiscal policy that expenditures be made in the most efficient way possible. As the President said in his budget message, "We must not allow expenditures to rise of their own momentum, without regard to value received." "It is my determined purpose," the President said, "to be a prudent steward of the public funds -- to obtain a dollar's worth of results for every dollar we spend."

The Federal budgeting process is not only one of deciding which programs shall be supported and which denied. It is also a process of maximizing results per dollar of funds spent. I regard this as a major and continuing responsibility of the Budget Bureau. We must lead a continuing, government-wide effort to increase efficiency and reduce waste.

The existence of such waste in recent years has, I know, been documented in studies carried out by congressional committees, including a subcommittee of this Committee. I hope it will be possible for us to continue to benefit from the interest of these committees, and that we can work together to bring about greater efficiency and economy of operation in all Government activities.

There are certain legislative actions which I hope will be taken this year to assist in this effort. Appropriated funds can be spent most efficiently if the Department head has authority to exercise some discretion in assigning funds and personnel within his agency. The President has asked the Congress, in enacting appropriations for each Department and agency, to provide the necessary authority to transfer within his agency a modest amount of the funds available for operating expenses, subject to control by the Bureau of the Budget through the regular apportionment process. Further, enactment of the bill (already passed by the Senate) giving the President authority to transmit reorganization plans to the Congress will strengthen the arm of the President in seeking efficiency and economy.

At the same time, I think it is clear that the task of driving out waste and improving efficiency is primarily a task of intelligent and continuous good management, acting day after day and month after month to find opportunities for improvement and put those improvements into effect. This is principally a matter of Executive Branch leadership, and I know -- and the President knows -- that a tremendous amount can be done within the authority already given by the Congress. I can assure you that the President takes a keen personal interest in this matter, and that we intend to keep steady pressure on every agency, and to follow up every lead that may promise better and cheaper results in the expenditure of public funds. The President has arranged for the continuing services of a group of distinguished consultants, including Robert Lovett and Don K. Price, to assist in the effort to achieve steady improvement in the effectiveness of Government operations. We expect to continue to give this matter top priority.

EXECUTIVE OFFICE OF THE PRESIDENT
BUREAU OF THE BUDGET
WASHINGTON 25, D. C.

March 27, 1961

DETAILS IN SUPPORT OF THE STATEMENT OF THE DIRECTOR OF THE BUREAU OF THE BUDGET

Total budget expenditures for fiscal 1961 are now estimated to be $80.7 billion, $1.7 billion higher than the January budget estimate of $78.9 billion. For fiscal 1962, budget expenditures are estimated to total $83.6 billion, which is $2.7 billion more than estimated in the January budget. Revised estimates of expenditures and needed new obligational authority for each functional program area in 1961 and 1962 are compared with the January budget estimates in Tables 5 and 6. (The estimates are shown for each major agency in Tables 16 and 17.) The figures for fiscal year 1962 exclude any changes to be proposed in the President's message on national defense, which is expected this week.

The largest single increase in estimated 1962 expenditures is for labor and welfare programs, which are expected to increase by $1,261 million, mainly for aid to education and for the temporary extended unemployment benefit program. Expenditures in 1962 for agriculture and agricultural resources are now expected to be $642 million higher than the January estimate; this increase reflects an upward revision in estimated disbursements for the program proposed by the preceding administration as well as the new proposals advanced in recent weeks by the President. An increase of $443 million is estimated for commerce and housing programs, and space technology, mainly for housing programs.

TABLE 5. BUDGET EXPENDITURES BY FUNCTION

(Fiscal years. In millions)

Function	1961 January estimate	1961 Current revision	1962 January estimate	1962 Current revision
Major national security	$45,930	$46,720	$47,392	1/$47,472
International affairs and finance	2,310	2,435	2,712	2,826
Commerce, housing, and space technology	3,784	3,950	3,371	3,814
Agriculture and agricultural resources	4,936	4,905	5,101	5,743
Natural resources	1,951	2,045	2,138	2,162
Labor and welfare	4,483	5,089	4,759	6,020
Veterans services and benefits	5,227	5,239	5,296	5,301
Interest	8,993	8,993	8,593	8,693
General government	1,982	1,968	2,071	2,095
Allowance for contingencies	25	25	100	100
Subtotal	79,621	81,369	81,532	84,226
Deduct interfund transactions	676	676	667	667
Total	78,945	80,693	80,865	83,559

1/ Excludes any program changes in the military functions of the Department of Defense to be proposed in President's defense message.

Notes: If the Congress adopts the President's proposal for a revolving fund for foreign aid loans, total loan disbursements will not change but the recorded totals of budget receipts and expenditures in 1962 would each be reduced by about $300 million.

Detail may not add to totals because of rounding.

TABLE 6. NEW OBLIGATIONAL AUTHORITY BY FUNCTION

(Fiscal years. In millions)

Function	1961 January estimate	1961 Current revision	1962 January estimate	1962 Current revision
Major national security	$45,912	$45,975	$46,278	1/$46,108
International affairs and finance	3,207	3,563	3,102	3,210
Commerce, housing and space technology	4,612	5,460	3,993	4,900
Agriculture and agricultural resources	4,696	7,238	4,605	5,285
Natural resources	2,049	2,050	2,012	2,109
Labor and welfare	4,937	6,171	5,025	6,442
Veterans services and benefits ..	5,438	5,438	4,963	5,003
Interest	8,993	8,993	8,593	8,693
General government	2,073	2,102	2,096	2,120
Allowance for contingencies	150	150	200	200
Total	82,068	87,141	80,867	84,072

1/ Excludes any program changes in the military functions of the Department of Defense to be proposed in President's defense message.
Note: Detail may not add to totals because of rounding.

Major National Security. Developments to date indicate that the January estimate of 1961 expenditures for the military functions of the Department of Defense, $41.5 billion, was an underestimate. A more realistic figure is $42.2 billion, an increase of $744 million. Part of this increase is offset by reductions of $200 million in the estimate of military assistance expenditures and $10 million for stockpiling expenditures, compared with the figures included in the January budget. Apart from reestimates, an increase of $256 million is estimated in 1961 expenditures for the military functions of the Department of Defense, primarily as a result of accelerations directed by the President. Of this increase, $175 million reflects speedier contract payments due to the lifting of the 20 percent holdback restriction that was placed on procurement contracts in 1957. The remainder is mainly for acceleration of the Polaris missile programs and the step-up in the rate of airlift modernization.

In total, the result of the reestimates of the January budget figures and the actions of the President is that budget expenditures for major national security programs in 1961 are now estimated to be $46.7 billion, an increase of $790 million over the January estimate.

For fiscal year 1962, the January budget program for the military functions of the Department of Defense has been reestimated upward by $190 million, reflecting a higher operating level consistent with the revised estimate for 1961. Partly offsetting this increase are declines of $100 million in military assistance expenditures and of $10 million for atomic energy programs. The 1962 figures do not include the effects of the President's new recommendations concerning defense, to be transmitted to the Congress shortly.

TABLE 7. MAJOR NATIONAL SECURITY

(Fiscal years. In millions)

Description	Expenditures 1961 estimate	Expenditures 1962 estimate	New obligational authority 1961 estimate	New obligational authority 1962 estimate
January 16, 1961 budget program	$45,930	$47,392	$45,912	$46,278
Reestimates of budget program:				
Department of Defense - military:				
Military functions	744	190	--	--
Military assistance	-200	-100	--	--
Stockpiling and defense production	-10	--	--	--
Revised estimate, January budget program	46,464	47,482	45,912	46,278
Proposed program changes:				
Department of Defense - military:				
Military functions	256	1/	63	1/
Military assistance	--	--	--	-200
Atomic Energy Commission (new obligational authority is for linear electron accelerator)	--	-10	--	30
Current estimate	46,720	47,472	45,975	46,108

1/ Excludes any program changes to be proposed in President's defense message.

International Affairs and Finance. Compared with the January budget, expenditures for international programs are currently estimated to be $2,435 million in fiscal year 1961, an increase of $125 million, and $2,826 million in fiscal 1962, an increase of $114 million.

For 1961, $50 million of the increase represents a reestimate of the net expenditures of the Export-Import Bank, reflecting the current expectation that loan disbursements will be higher and loan repayments lower than estimated in the January budget. Another $50 million, similarly, reflects a reestimate of mutual security (economic and contingencies) expenditures, again based on the latest information available. It is estimated that $25 million will be spent this year under the $100 million supplemental appropriation requested for Chilean reconstruction; no estimate for this purpose was carried in the January budget.

The estimated increase in expenditures for fiscal year 1962 includes (1) $50 million representing a reestimate of the expenditures for the Inter-American Program for Social Progress, (2) $50 million for the Chilean reconstruction program, and (3) $14 million for the State Department (mainly for Africa) and U. S. Information Agency (expansion of activities in Africa and Latin America).

New expenditures of $20 million for the Peace Corps can be included within the amounts previously estimated for foreign economic assistance, because of the expectation that other aid disbursements will decline temporarily as emphasis shifts from support aid to planned investment programs abroad.

TABLE 8. INTERNATIONAL AFFAIRS AND FINANCE

(Fiscal years. In millions)

Description	Expenditures 1961 estimate	Expenditures 1962 estimate	New obligational authority 1961 estimate	New obligational authority 1962 estimate
January 16, 1961 budget program........	$2,310	$2,712	$3,207	$3,102
Reestimates of budget program:				
Export-Import Bank....................	50	--	--	--
Mutual security - economic and contingencies..........................	50	--	--	--
Inter-American Program for Social Progress............................	--	50	--	--
Revised estimate, January budget program............................	2,410	2,762	3,207	3,102
Proposed program changes:				
Chilean reconstruction................	25	50	100	--
Emergency famine relief (Commodity Credit Corporation)................	--	--	256	-115
Mutual security - economic and contingencies (including Peace Corps)................................	--	1/	--	200
State Department (mainly for Africa)...............................	--	6	--	12
United States Information Agency......	--	8	--	11
Current estimate...............	2,435	2,826	3,563	3,210

1/ If the Congress adopts the President's proposal for a revolving fund for foreign aid loans, total loan disbursements will not change but the recorded expenditures in 1962 would be reduced by about $300 million.

<u>Commerce, Housing, and Space Technology</u>. The current outlook is for an increase over the January budget estimate of $166 million, to $3,950 million, in 1961 expenditures for commerce and housing programs, and for space technology. The major change is in the postal deficit, reflecting the now obvious fact that postal rate increases will not be enacted effective April 1, 1961, as assumed in the January budget estimate. Expenditures for Veterans Administration direct housing loans from funds already available will apparently run some $74 million higher than estimated in January as a result of continued high demand and improved loan processing procedures. These and other increases are offset in part by a downward revision of $50 million in the January estimate of expenditures for space programs.

Budget expenditures in 1962 are now estimated to increase by $443 million over the January estimate, from $3,371 million to $3,814 million, largely for housing programs, for redevelopment of distressed areas, and for acceleration of research and development in selected space activities. In addition to the legislative proposals for housing programs, made in the President's message to the Congress of March 9, the revised estimate reflects accelerated activity under prior authorizations in public facility loans, college and veterans housing loans, and urban renewal.

The current estimate of 1962 expenditures assumes that the Congress will act, as the President is recommending, to increase postal rates effective July 1, 1961, by enough to eliminate the postal deficit now in prospect for 1962 under present rates.

TABLE 9. COMMERCE, HOUSING, AND SPACE TECHNOLOGY

(Fiscal years. In millions)

Description	Expenditures 1961 estimate	Expenditures 1962 estimate	New obligational authority 1961 estimate	New obligational authority 1962 estimate
January 16, 1961 budget program........	$3,784	$3,371	$4,612	$3,993
Reestimates of budget program:				
Post Office..........................	140	--	148	--
Veterans Administration direct housing loans......................	74	--	--	--
Office of Civil and Defense Mobilization......................	11	--	--	--
Federal Aviation Agency..............	-10	3	--	12
National Aeronautics and Space Administration......................	-50	--	--	--
Housing and Home Finance Agency......	-30	--	--	--
Other................................	-10	--	--	--
Revised estimate, January budget program............................	3,909	3,374	4,760	4,005
Proposed program changes:				
Housing and Home Finance Agency:				
College housing loans..............	11	45	100	150
Low-cost housing...................	--	65	--	350
Urban renewal......................	--	54	600	-300
Public facility loans..............	--	30	--	50
Housing for the elderly............	--	10	--	50
Other..............................	--	10	--	120
Farm housing loans...................	30	45	--	225
Veterans Administration direct housing loans......................	--	30	--	--
National Aeronautics and Space Administration......................	--	85	--	126
Area redevelopment...................	--	40	--	42
Federal Aviation Agency..............	--	10	--	47
Coast Guard..........................	--	8	--	13
Department of Commerce (scientific research and other programs)........	--	8	--	23
Current estimate................	3,950	3,814	5,460	4,901

Agriculture and agricultural resources. Budget expenditures for agricultural programs are now expected to be $4,905 million in 1961 and $5,743 million in 1962. The present estimate for 1961 is $31 million less than the January estimate, primarily because of a $423 million reduction in the estimated expenditures of the Commodity Credit Corporation for farm price supports and related activities. Largely offsetting this decrease are program changes made by this administration. The largest increases are $225 million in Commodity Credit Corporation expenditures under the new feed grain legislation and $118 million for the domestic distribution of increased amounts of surplus foods; another $34 million is for increased farm ownership and operating loans over the level contemplated in the previous administration's program.

For the fiscal year 1962, total expenditures are now estimated to be $642 million higher than the January estimate. It now appears that the January budget program for the Commodity Credit Corporation was underestimated by $249 million. Even at the low support levels assumed in the 1962 budget, lower exports, reduced domestic consumption, and higher crop yields than were estimated when the January budget calculations were made can now be expected to increase outlays for farm price and income supports and other activities. A larger increase of $393 million in 1962 expenditures will result from program changes proposed by the President, including those described in his agricultural message of March 16. Details are shown in the following table.

TABLE 10. AGRICULTURE AND AGRICULTURAL RESOURCES

(Fiscal years. In millions)

Description	Expenditures 1961 estimate	Expenditures 1962 estimate	New obligational authority 1961 estimate	New obligational authority 1962 estimate
January 16, 1961 budget program.......	$4,936	$5,101	$4,696	$4,605
Reestimates of budget program:				
Commodity Credit Corporation........	-423	249	--	--
Soil Bank program..................	11	--	--	--
Revised estimate, January budget program..............................	4,524	5,350	4,696	4,605
Proposed program changes:				
Commodity Credit Corporation (price supports: cotton, peanuts, rice, and milk; surplus food distribution abroad and other).............	225	164	2,542	507
Surplus food distribution (domestic)	118	100	--	--
Food stamp pilot program...........	4	50	--	--
Farm ownership and operating loans..	34	77	--	84
Rural Electrification Administration loans..........................	--	15	--	100
Other..............................	--	-13	--	-11
Current estimate..............	4,905	5,743	7,238	5,285

Natural Resources. Expenditures in the fiscal year 1961 for natural resources programs are now estimated to be $94 million above the January budget estimate. The current estimate of $2,045 million includes the expenditure of $69 million by the Forest Service to pay for those forest lands of the Klamath Indians which are not sold to competitive bidders by April 1, 1961. The January budget provided for a supplemental appropriation for 1961 to cover this payment, which is required by law, but proposed unjustifiably to defer the payment until fiscal year 1962. This shift of expenditures from 1962 back to 1961 offsets a number of expenditure increases proposed by the President for 1962, so that the total rise in natural resources expenditures in the coming fiscal year as compared with the budget estimate is $24 million.

The increases for 1962, as shown in the following table, are for certain activities which are being accelerated, particularly for development of our national forests, parks, and seashore and recreational areas; for construction of Indian schools; and for starting some new water resource projects of the Corps of Engineers. In addition, the Bureau of Reclamation will initiate construction of additional transmission lines and will continue construction of one new project which is being started, at the direction of the President, in fiscal 1961. These and other measures set forth in the President's message of February 23 will make possible greater progress toward the Nation's long-range resource conservation and development goals.

TABLE 11. NATURAL RESOURCES

(Fiscal years. In millions)

Description	Expenditures 1961 estimate	Expenditures 1962 estimate	New obligational authority 1961 estimate	New obligational authority 1962 estimate
January 16, 1961 budget program	$1,951	$2,138	$2,049	$2,012
Reestimates of budget program:				
Klamath Indian land purchase	69	-69	--	--
Corps of Engineers, construction	25	20	--	--
Tennessee Valley Authority	-15	--	--	--
Other	-10	--	--	--
Revised estimate, January budget program	2,020	2,089	2,049	2,012
Proposed program changes:				
Bureau of Indian Affairs (Indian welfare and education)	1	14	--	21
National Park Service (Mission 66 and seashore areas)	4	11	--	20
Other Interior Department	5	8	1	11
Forest Service	--	21	--	21
Corps of Engineers, construction	15	17	--	22
Tennessee Valley Authority	--	2	--	2
Current estimate	2,045	2,162	2,050	2,109

Labor and Welfare. Budget expenditures for education, labor, health, and welfare programs in 1961 are now estimated to be $5,089 million, $606 million more than the January estimate. For 1962, the current estimate is $6,020 million, an increase of $1,261 million from the January budget.

Almost all the increase in 1961 is for temporary extended unemployment benefits and aid to dependent children of the unemployed. Budget expenditures of $574 million are estimated for 1961 for the temporary unemployment compensation program, representing an advance to the unemployment trust fund. This amount includes extended benefits for unemployed railroad workers, and for Federal employees and ex-servicemen. Disbursements to the States under this temporary program will be made from the trust fund in 1961 and 1962, and the advance will be repaid to the Treasury in later years from increased proceeds of the Federal unemployment tax.

The largest single expenditure increase estimated for 1962 is $500 million for the elementary and secondary school program proposed in the President's education message to the Congress on February 20. Another $440 million is for the 1962 advance to the unemployment trust fund for the temporary unemployment compensation program. The proposed legislation to aid dependent children of the unemployed is estimated to entail expenditures of $215 million in 1962. Proposed legislation and budgetary increases in other programs for health, science and scientific research, education, and welfare would increase spending in 1962 by an additional $106 million. This estimate reflects an anticipated reduction of $52 million in the January estimate of budget expenditures for public assistance, which would result from enactment of the proposals for liberalizing the old-age, survivors, and disability insurance program and for providing medical care for the aged through the social security system.

TABLE 12. LABOR AND WELFARE

(Fiscal years. In millions)

Description	Expenditures 1961 estimate	Expenditures 1962 estimate	New obligational authority 1961 estimate	New obligational authority 1962 estimate
January 16, 1961 budget program.........	$4,483	$4,759	$4,937	$5,025
Reestimates of budget program:				
National Science Foundation..........	-10	-10	---	---
Other................................	---	-1	---	-1
Revised estimate, January budget program............................	4,473	4,748	4,937	5,024
Proposed program changes:				
Temporary extended unemployment compensation.......................	550	440	990	---
Temporary extended railroad unemployment benefits.......................	24	---	24	---
Advances for employment security administration.......................	14	-10	18	20
Elementary and secondary education....	---	500	---	667
Aid to higher education..............	---	21	---	332
Aid to federally affected schools.....	---	-5	---	8
National defense education...........	---	32	---	82
Aid to dependent children of the unemployed.........................	28	215	30	226
OASDI liberalization and medical care (budget effect)..................	---	-52	---	-52
Public Health Service:				
Medical education and research.......	---	9	---	34
Community health activities..........	---	9	---	24
Water and air pollution control......	---	12	---	52
Other Public Health Service (mainly National Institutes of Health)........................	---	38	1	80
Maternal and child welfare grants.....	---	10	---	10
National Science Foundation--grants for basic research and science education...........................	---	29	---	65
School lunch program..................	---	10	---	10
Special milk program..................	---	9	171	-161
Vocational rehabilitation and other...	---	9	---	21
Current estimate..................	5,089	6,020	6,171	6,442

Veterans Services and Benefits. Budget expenditures for veterans programs are currently estimated to be $5,239 million in fiscal 1961, $12 million higher than estimated in January, and to be $5,301 million in 1962, a rise of $5 million from the January budget estimate. The revision for 1961 is a reestimate of the January budget program, based on actual trends to date. The estimated 1962 expenditures reflect the net effect of (1) a downward reestimate of the January figures, mainly due to a lesser than anticipated impact of the Veterans Pension Act of 1959, which liberalized eligibility requirements and raised pension rates for many pensioners on the rolls, and (2) a proposed selective increase in compensation rates for veterans with severe service-connected disabilities to offset rises in the cost of living since rates were last adjusted in 1957 and to adjust some rates which are out of line.

TABLE 13. VETERANS SERVICES AND BENEFITS

(Fiscal years. In millions)

Description	Expenditures 1961 estimate	Expenditures 1962 estimate	New obligational authority 1961 estimate	New obligational authority 1962 estimate
January 16, 1961 budget program.........	$5,227	$5,296	$5,438	$4,963
Reestimates of budget program:				
Veterans compensation and pensions....	--	-40	--	-25
Other Veterans Administration programs	12	-20	--	--
Revised estimate, January budget program..............................	5,239	5,236	5,438	4,938
Proposed program changes:				
Selective increase in compensation rates........................	--	65	--	65
Current estimate............	5,239	5,301	5,438	5,003

Interest. Expenditures for interest in 1962 are now estimated to be $8,693 million, an increase of $100 million over the January estimate. This is due to increased interest on the public debt growing mainly out of the heavier borrowing in 1961 and 1962 now expected.

TABLE 14. INTEREST

(Fiscal years. In millions)

Description	New obligational authority and expenditures: 1961 estimate	New obligational authority and expenditures: 1962 estimate
January 16, 1961 budget program...............	$8,993	$8,593
Reestimates of budget program:		
Interest on the public debt.................	—	100
Current estimate...................	8,993	8,693

General Government. Expenditures in fiscal year 1961 for general government activities are currently estimated to be $1,968 million, which is $14 million less than estimated last January. For fiscal year 1962, the current estimate is $2,095 million, an increase of $24 million over the estimate in the January budget. The major changes in the 1961 estimate are for higher unemployment compensation payments to ex-servicemen and former Federal employees, more than offset by downward revisions in the estimates for the General Services Administration and other agencies in this category.

TABLE 15. GENERAL GOVERNMENT

(Fiscal years. In millions)

Description	Expenditures 1961 estimate	Expenditures 1962 estimate	New obligational authority 1961 estimate	New obligational authority 1962 estimate
January 16, 1961 budget program........	$1,982	$2,071	$2,073	$2,096
Reestimates of budget program:				
Unemployment compensation for Federal employees and ex-servicemen..........................	33	--	33	--
General Services Administration......	-42	--	--	--
Other................................	-25	--	-6	--
Revised estimate, January budget program..............................	1,948	2,071	2,100	2,096
Proposed program changes:				
Judgeship Bill.......................	--	4	--	4
Treasury Department..................	--	17	1	17
Other................................	20	3	1	3
Current estimate............	1,968	2,095	2,102	2,120

TABLE 16. BUDGET EXPENDITURES BY MAJOR AGENCY

(Fiscal years. In millions)

Agency	1961 January estimate	1961 Current revision	1962 January estimate	1962 Current revision
Legislative branch and the judiciary...	$208	$200	$203	$207
Executive Office of the President......	61	72	92	92
Funds appropriated to the President:				
Mutual security--economic and contingencies........................	1,675	1,725	1,875	1,875
Other..................................	43	58	75	175
Independent offices:				
Atomic Energy Commission.............	2,660	2,660	2,680	2,670
Export-Import Bank...................	-100	-50	-4	-4
Federal Aviation Agency..............	640	630	730	743
National Aeronautics and Space Administration.......................	770	720	965	1,050
Veterans Administration..............	5,314	5,400	5,369	5,404
Other..................................	770	759	676	704
General Services Administration........	442	420	496	498
Housing and Home Finance Agency........	544	525	728	942
Department of Agriculture..............	5,739	5,807	5,782	6,440
Department of Commerce.................	511	511	566	614
Department of Defense--Military:				
Military functions...................	41,500	42,500	42,910	1/43,100
Military assistance..................	1,700	1,500	1,750	1,650
Department of Defense--Civil...........	986	1,015	984	1,021
Department of Health, Education, and Welfare..........................	3,716	3,744	4,005	4,798
Department of the Interior.............	785	785	873	906
Department of Justice..................	285	285	294	296
Department of Labor....................	295	892	223	654
Post Office Department.................	786	926	63	63
Department of State....................	260	260	345	351
Treasury Department:				
Interest.............................	8,993	8,993	8,593	8,693
Other................................	965	965	1,095	1,120
District of Columbia...................	48	42	66	66
Allowance for contingencies............	25	25	100	100
Subtotal...........................	79,621	81,369	81,532	84,226
Deduct interfund transactions..........	676	676	667	667
Total..............................	78,945	80,693	80,865	83,559

1/ Excludes any program changes to be proposed in President's defense message.
Note: Detail may not add to totals because of rounding.

TABLE 17. NEW OBLIGATIONAL AUTHORITY BY MAJOR AGENCY

(Fiscal years. In millions)

Agency	1961 January estimate	1961 Current revision	1962 January estimate	1962 Current revision
Legislative branch and the judiciary...	$176	$176	$180	$184
Executive Office of the President......	72	72	116	116
Funds appropriated to the President:				
Mutual security--economic and contingencies......................	2,131	2,131	2,200	2,400
Other.............................	507	607	13	13
Independent offices:				
Atomic Energy Commission............	2,781	2,781	2,598	2,628
Federal Aviation Agency.............	690	690	686	745
National Aeronautics and Space Administration......................	965	965	1,110	1,236
Veterans Administration.............	5,577	5,577	5,101	5,141
Other...............................	756	780	755	832
General Services Administration........	520	521	556	558
Housing and Home Finance Agency........	1,119	1,819	948	1,368
Department of Agriculture..............	5,361	8,330	5,509	6,169
Department of Commerce.................	549	549	612	677
Department of Defense--Military:				
Military functions..................	41,308	41,371	41,840	1/41,840
Military assistance.................	1,800	1,800	1,800	1,600
Department of Defense--Civil...........	978	978	972	994
Department of Health, Education, and Welfare..........................	3,909	3,940	4,026	5,505
Department of the Interior.............	837	838	888	940
Department of Justice..................	297	297	297	299
Department of Labor....................	525	1,566	264	289
Post Office Department.................	728	876	63	63
Department of State....................	268	268	351	363
Treasury Department:				
Interest............................	8,993	8,993	8,593	8,693
Other...............................	992	993	1,126	1,156
District of Columbia...................	79	73	63	63
Allowance for contingencies............	150	150	200	200
Total........................	82,068	87,141	80,867	84,072

1/ Excludes program changes to be proposed in President's defense message.
Note: Detail may not add to totals because of rounding.

Airmail

March 27, 1961.

Dear Bob:

Thank you for your nice note of March 24 and I am glad you approve of my statement before the Joint Economic Committee. We will continue to do our best and all of us here are most appreciative of the service you are rendering to the Dallas Bank.

With all good wishes,

Cordially yours,

Wm. McC. Martin, Jr.

Mr. Robert O. Anderson,
Box 660,
Roswell, New Mexico.

ROBERT O. ANDERSON
BOX 660
ROSWELL, NEW MEXICO

Mr. William M. Martin, Jr.
Federal Reserve System
Board of Governors
Washington, D. C.

Dear Bill:

Just a note to let you know how much I enjoyed your excellent statement made before the Joint Economic Committee on the 7th of March. I think you are starting to get your message across to Congress in a way that the System has never been able to do in the past.

Public awareness is now sufficient that even our Congressmen are realizing they will be asked questions about gold, interest, etc., and are expected to give reasonable answers or explanations. I think you have proved that persistance can finally win out even in Washington!

Regards,

Bob

March 24, 1961

Miss Muehlhaus

March 24, 1961

Mr. N. S. Anon
Department of Public Affairs
International Business Machines Corp.
590 Madison Avenue
New York 22, N. W.

Dear Mr. Anon:

Thank you for your nice letter of March 20. You will find enclosed a copy of the statement you wanted to see. Incidentally, that was an interesting remark you made to the effect that "an approach is necessary which lies between that of the classical economists and that of Keynes."

Sincerely yours,

(SIGNED) WM. McC. MARTIN, JR.

Wm. McC. Martin, Jr.

Enclosure
CM:nk

cc: Miss Muehlhaus

FOR FILES
M. Muehlhaus

Mr. Molony

INTERNATIONAL BUSINESS MACHINES CORPORATION
590 MADISON AVENUE
NEW YORK 22, N.Y.

DEPARTMENT OF PUBLIC AFFAIRS

March 20, 1961

Mr. William Mc. Martin
Chairman Federal Reserve Board
Washington 25, D. C.

Dear Mr. Martin:

I would appreciate your sending me a copy of your recent testimony before the joint economic committee.

I was delighted to read in the New York Times a brief description of your approach. From what I can see it is one that I am in strong agreement with, believing that the unemployment situation represents a structural imbalance of the economy, and can not be ameliorated by aggregative policies.

In essence it appears to me that an approach is necessary which lies between that of the classical economists and that of Keynes.

Thanks very much.

Yours truly,

N. S. Anon

NSA/ic

Miss Muehlhaus

March 21, 1961

Mr. J. D. Maurice, Editor
The Charleston Daily Mail
Charleston 30, West Virginia.

Dear Mr. Maurice:

Thank you for your nice letter of March 16 and for the copy of the Charleston Daily Mail editorial of March 13 which contains references to my comments to the Joint Congressional Economic Committee.

The editorial struck me as measuring up fully to your editorial page motto: "Without, Or With, Offence To Friends Or Foes, I Sketch Your World Exactly As It Goes." It is a pleasure to have one's views summarized in so straightforward a context.

Although I do not recall making reference to a particular study, extensive information on the seriousness of the problem of persistent unemployment attributable to changes in economic structure has been furnished to and by Congressional Committees in recent times. Hearings are being held presently by the House Education and Labor Subcommittee on Unemployment and the Impact of Automation, and by the Senate Labor and Public Welfare Subcommittee on Education (on the retraining of persons displaced from their jobs because of structural changes in the economy.) In addition, you might find material of interest to you in such committee publications as the following:

Senate Special Committee on Unemployment Problems - 86th Congress, 2nd Session, 1960. S. Resolution #196
- a) Studies in Unemployment
- b) Report of the Committee
- c) Part 6 - Hearings

Committee on Banking and Currency, Subcommittee on Production and Stabilization.
- a) Area Development - 1961 (Hearings)
- b) Report of the Committee on Banking and Currency - on S 1
- c) Also hearings and Reports on Area Redevelopment - 1959-1960

Joint Economic Committee
a) New Views on Automation 1960
b) The Structure of Unemployment 1960 in Areas of Substantial Labor Surplus, Study Paper No. 23

Incidentally, I'm sure it was of interest to you, as it was to me, to note the President's remarks on unemployment at his news conference on March 15, in which he referred specifically to West Virginia and other areas, as shown on the attached clipping from the transcript of that conference.

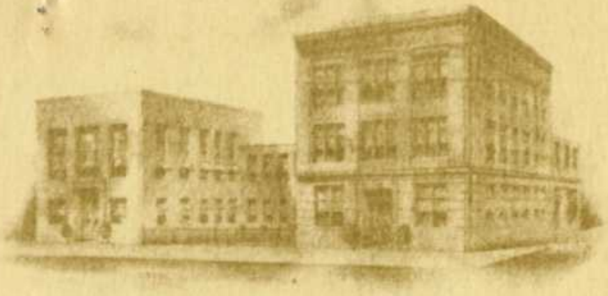
Sincerely yours,

(SIGNED) WM. McC. MARTIN, Jr.

Wm. McC. Martin, Jr.

Enclosure
CM:nk
cc: Miss Muehlhaus

Mr. Molony



The Charleston Daily Mail

PUBLISHED BY
THE CHARLESTON MAIL ASSOCIATION
CHARLESTON 30, WEST VIRGINIA

March 16, 1961

Mr. William McC. Martin, Chairman
Board of Governors of the Federal Reserve System
Federal Reserve Building
Constitution Avenue
Washington, D. C.

Dear Mr. Martin:

As a West Virginia editor I am deeply and directly interested in the problem of "structural" unemployment which you discussed last week in your appearance before the Joint Congressional Economic Committee. My own informal and fractional studies compel me to the conclusions which you have expressed: That long after the national economy has made a satisfactory recovery, West Virginia's problem will remain, and that attempts to solve it by massive and imprecise inflationary means will certainly do more harm than good.

It is for this reason that I am taking the liberty of sending you an editorial inspired, in part, by your testimony and referring to the efforts of Mayor Francis of Huntington to initiate some action along the lines you suggest. Our problem, as you may gather, is to arouse some interest where so much of the curative effort seems to be directed toward inadequate and often demoralizing relief or a permanent inflation. So far, I am sorry to say, we have not generated much enthusiasm for attacking this problem at its source, which is the displaced (as distinguished from the unemployed) miner.

I thought you might be interested to know that some of us in West Virginia have been thinking along the same lines.

Incidentally, if copies of the Federal Reserve study to which you have referred are available, I would greatly appreciate one.

Sincerely,

J. D. Maurice

JDMaurice/mjb
Enclosure

This article is protected by copyright and has been removed.

Article Title: Prime The Pump Or Train The Individual; Which Is The Better Road To Recovery?

Journal Title: Charleston Daily Mail

Date: March 13, 1961

March 21, 1961.

Dear Frazar:

Thank you for your nice letter of March 15 with respect to my testimony before the Joint Economic Committee.

I am glad you approve of it and you are quite right that time limitation required omission of the voluntary credit control and other activities during the period. My comments were directed entirely to open market operations and the evolution of "bills preferably." But I certainly agree with you as to the importance of the other elements.

With all good wishes,

Cordially yours,

Wm. McC. Martin, Jr.

Mr. Frazar B. Wilde,
Chairman of the Board,
Connecticut General Life Insurance Company,
Hartford, Connecticut.

Hartford, Connecticut

CONNECTICUT GENERAL
LIFE INSURANCE COMPANY

Frazar B. Wilde, Chairman of the Board

March 16, 1961

Dear Bill:

Your statement to the Joint Economic Committee on March 7 not only reads well but it makes good sense! I was particularly interested in the history you traced because I played a very minor role in some of it.

The somewhat abortive yet interesting work of the committees on voluntary credit control you did not mention in your statement. I presume you were properly concerned with the need for brevity.

To me it was valuable experience in learning about the practical difficulties of selective credit controls and, at the same time, I might add that standby controls are not necessarily condemned because of that experience.

Sincerely yours,

Frazar

The Honorable William McChesney Martin, Jr.
Chairman, Board of Governors
Federal Reserve System
Washington, D. C.

CHARLES J. CHANDLER

WICHITA, KANSAS

March 21, 1961

Mr. Wm. McC. Martin, Jr.
Board of Governors of the
Federal Reserve System
Washington, D. C.

Dear Bill:

I have your kind note of March 17th which I did not expect you to bother to answer. I appreciated greatly the opportunity to read in detail the statements you made before the Joint Economic Committee on March 7th. Bob Bethke attended the Committee hearing and I had a visit with him about it and I, of course, read the condensed statements in the Goldsmith-Nagen Letters which had more to do with the questions and answers period than the statements themselves.

I am especially glad that you brought out the matter of the structural type of unemployment, because it is this which is going to be the hardest to lick, in my opinion, and is the sort of thing that money alone cannot buy. Your thinking, as always, is sound and I feel as you do -- that to make water run up and down hill at the same time requires a very unusual situation.

I want to say in closing that I think you handled Representative Reuss' questioning excellently.

With my warmest regards,

Sincerely,

Charlie

C. J. Chandler

CJC:L

No need to respond.

Airmail

March 17, 1961.

Dear Charlie:

I do appreciate your note very much and it is good to hear from one's real friends. I am enclosing a copy of my statement before the Joint Economic Committee which you might enjoy glancing through.

My best, as always.

Cordially yours,

Wm. McC. Martin, Jr.

Mr. Charles J. Chandler,
First National Bank in Wichita,
Wichita, Kansas.

2701 O Street N. W.
Washington 7, D. C.
March 21, 1961

Hon. Wm. McC. Martin, Jr.
Chairman, Board of Governors
Federal Reserve System
Washington 25, D. C.

Dear Bill:

Thank you for sending me the manuscript of your Statement before the Joint Economic Committee. I have used it as the basis of a further letter to Dr. Neal, as per copy enclosed.

It may be that I am overconcerned with our present situation, but there are things in it which disturb me deeply.

Sincerely yours,

Ralph

Ralph E. Flanders

Enclosure

2701 O Street N. W.
Washington 7, D. C.
March 21, 1961

Dr. Alfred C. Neal, President
Committee for Economic Development
711 Fifth Avenue
New York 22, New York

Dear Al:

This is a continuation on the subject of my letter o f February 21.

Do you have access to Chairman Martin's statement before the Joint Economic Committee of March 7, 1961? If so, I would call your attention to the passage beginning with the last two paragraphs on page 16, in which he considers the problem of "structural unemployment." This particular passage ends with the third full paragraph on page 18, in which he says, "Meanwhile there is, I think, need on the part of all of us to recognize that the world in which we live today is not only a world that has changed greatly in recent years, but also a world that even now is in a period of further transition."

It seems to me that Mr. Martin underscores the points of view I have been trying to make, though I would by no means assume that he would be in full agreement with the points of view I have raised.

He suggests that actions best suited to helping the structurally unemployed would include "more training and re-training to develop skills needed in expanding industries." One of the fundamental questions I am raising, of course, is the question as to whether industries are expanding as fast, whether in variety or employment, as is the total number of employables. We have accepted the axiom that employment, production and consumption can be expected under normal conditions to keep in step with each other. Maybe that is an axiom which needs to be questioned.

Sincerely yours,

Ralph E. Flanders

cc: Donald K. David
W. McC. Martin, Jr.

March 20, 1961.

The Honorable Ralph E. Flanders,
2701 O Street, N. W.,
Washington 7, D. C.

Dear Senator:

Thank you for your nice letter of March 8. As you know, the newspapers with their limited space are not always able to reflect adequately the content of a statement as long as mine was to the Joint Economic Committee. For that reason a copy of the full text is enclosed that should help to clarify my comments.

You will see that I was emphasizing that there are really these two types of unemployment--structural and cyclical. In my view we need to be doing a good deal about both types. However, I am in agreement with you that we are facing new conditions for which there is no precedent and we must attack this hard core "structural" unemployment in a different way than we have done before.

Here at the Fed we have been doing everything we can to help in the revival of business conditions and this will assist in remedying cyclical unemployment. It is asking too much, I believe, to expect monetary and credit policy to be very helpful in working out the problems of structural unemployment.

I was interested in the extracts from your letter to Dr. Neal. The Committee for Economic Development has long served a useful purpose and we all hope it will continue to do so. It is good that persons like yourself are trying to keep it on its toes.

Sincerely yours,

(Signed) Bill M.

Wm. McC. Martin, Jr.

Enclosure.
CLF:rem
cc: Miss Muehlhaus
Miss Morris

Mr. Farmer

(M)

2701 O Street N. W.
Washington 7, D. C.
March 8, 1961

Honorable William McChesney Martin, Jr.
Chairman, Board of Governors
Federal Reserve System
Federal Reserve Building
Washington 25, D. C.

Dear Friend Martin:

The morning paper reports that you have characterized the present unemployment as being of a "built in" type. Does this mean that in your judgment we are facing new conditions for which there is no precedent?

I have been coming to that conclusion myself and in talking with Don David a short time ago expressed my fear that my old organization the CED was skating over the surface of economic problems instead of dealing with fundamentals. He suggested that I write to Dr. Neal and send him a copy. That I did.

Enclosed herewith for your personal consideration are some personal extracts from my long letter. I would be glad indeed of any comment you may wish to make on the point of view therein expressed.

Sincerely yours,

Ralph E. Flanders

Ralph E. Flanders

Enclosure

EXTRACTS

From a Letter Dated February 21, 1961

To Dr. Alfred Neal, President
Committee for Economic Development

. . . C. E. D. is in a rut which leads to nowhere. It must get out of it and go somewhere.

The world itself is not in a rut. It is striking out into the unknown, both politically and economically. It is with the economic changes that C. E. D. has its greatest responsibilities. Let me list some of the evidences that we are in new economic situations.

1. There is a new fluidity of technology, managerial ability and capital which tends toward the migration of manufacture to areas of low labor cost, under conditions which make labor cost the basic element in competition.

2. Productivity in our country is catching up with consumption, putting a premium on advertising and salesmanship to expand the consumption of sated consumers.

3. The unsatisfied needs of our nation are social, not individual--e.g., sewage treatment so that every flowing stream is safe to drink from. . . . . .

With regard to the selected problems listed above I offer the following observations. These are observations, not solutions. C. E. D. must address itself to solutions.

As suggested in item 1 above, we are living in a new age so far as concerns foreign competition. Modern production makes minimum demands on the skill of the individual worker, but maximum demands on technology and management. This fact makes it possible for the technology and management methods to be developed in high-wage America and then exported bodily to lower wage countries. This fact is the moving element in the immense volume of investment abroad which has taken place since the end of World War II. We cannot long continue to manufacture here and sell abroad. To compete in foreign markets we must manufacture abroad.

. . .

What is the answer to this problem? Is it higher duties or quotas? Or do we replace vanishing industries with others, new or old, in which we continue to have a competitive advantage? If so, what are those industries? Can we maintain that competitive advantage, and how? These matters were left unconsidered by the Randall Commission. In the act extending the reciprocal trade treaties I introduced an amendment calling for a new commission to go into the real problems of international trade. The Senate passed the amendment but it was lost in conference. The opportunity is still open to the C. E. D.

This whole subject is important in connection with our balance of trade situation. The recent report on this matter seemed to me to be broad and shallow. It rang all the changes on conventional economics without giving more than a sidewise glance at the deeper influences at work. I introduced into the discussion one of the fundamental elements--the division of the profits arising from improved business efficiency. Had these increments of profit in the last fifteen years been apportioned among higher wages, lower prices and increased profits, every element of our society would have benefited, including the wage earners; and the balance of trade could have been maintained. Unfortunately this is a matter of industry and labor morals--not of legislation; and the unfortunate effects of immoral practices are now deeply imbedded in our economy. Here is a problem!

As to item 2, we continue to expect that consumption will automatically keep pace with increased efficiency in production. Can we be sure of this much longer? Our reliance on a fantastic expansion of the advertising business raises doubts. Advertising failed to sell new models of standard cars in '59 and '60. The customers' demands were more modest. The smaller, more economical car was preferred and imports from Europe increased. Car owners no longer respond to the lure of prestige in design. They are becoming mature and discerning.

This maturity of the consumer is in evidence in other lines. A successful maker of household equipment reports that he no longer gets a customer response to new models with new gadget accessories. What is going to happen to the equipment industries if the consumer grows up? Employment will drop in production. Will the expansion of employment in advertising take up the slack?

Returning once more to the small car, its very design requires fewer labor hours to produce it. But this is only half the story. In the last 15 years the methods of production have been so mechanized and automated that a great reduction in labor hours is sufficient to produce a car whether it be large or small. Can we be sure that the consumer is now being financed by our enterprise system automatically and eagerly, or even reluctantly, to absorb the new production?

• • • • •

My third proposition is that the great opportunity for expanded consumption is not in the private but in the social sector of our economy. Sewage disposal and its twin, water conservation, are examples. So are school facilities at all levels. Here we are faced with a real problem. Our means for financing such projects is by taxing the personal profits of private business. There are limits to funds so collected and this limits the amount of socially desirable undertakings. In a nation with a labor surplus, a food surplus, a surplus capacity for providing clothing and shelter, the physical requirements for meeting expanded social consumption are all present. A totalitarian solution is theoretically able to organize society for a great social program. Can it be done by a private enterprise society? How?

. . . . .

There may be something deeper here than we have ever imagined. An intimation was given in a recent paper by Dr. Edwin Nourse, former chairman of the President's Economic Council, in which he speaks of our having arrived at a "hinge."

. . . . .

This letter is a compilation of problems which insistently demand solutions. I can offer no solutions but they must be sought and found. Will C. E. D. address itself to that task? If it is unable or unwilling, its usefulness is waning.

. . . . .

Ralph E. Flanders

March 20, 1961

Dear Wilfrid:

Thank you for sending me the March 16 issue of the Commercial and Financial Chronicle which reproduced my statement before the Joint Economic Committee. It is nice of you to bring it to my attention.

With all good wishes,

Cordially yours,

Wm. McC. Martin, Jr.

Mr. A. Wilfred May,
Executive Editor,
The Commercial and Financial Chronicle,
25 Park Place,
New York 7, New York.

Mi-s Muehlhaus

March 17, 1961

The Hon. David L. Francis
Mayor
City of Huntington
West Virginia.

Dear Mr. Francis:

Thank you for your nice letter of March 14 and for sending me a copy of your report, "Solving A Critical Human Problem." Also for the copy of the Charleston Daily Mail editorial, which certainly put me in good company.

I'm sure it was of interest to you, as it was to me, to note the President's remarks on unemployment at his news conference Wednesday, in which he referred specifically to "eastern Kentucky, West Virginia" and other areas, as shown on the attached clipping from the transcript of that conference.

Sincerely yours,

(SIGNED) WM. McC. MARTIN, Jr.

Wm. McC. Martin, Jr.

Enclosure
CM:nk
cc: Miss Muehlhaus

Molony

CITY OF HUNTINGTON

HUNTINGTON, WEST VIRGINIA

OFFICE OF THE MAYOR

March 14, 1961

Mr. William McC. Martin, Jr.
Chairman, Federal Reserve Board
Washington, D. C.

Dear Mr. Martin:

Attached herewith is a copy of an editorial appearing yesterday morning in the Charleston paper, in which both of our names were mentioned. I am flattered!

I am also attaching a summary of information which I have been using in conversations in Washington and in Charleston, our State Capitol, on this program. We need a lot of help to convince President Kennedy and those in command that this vocational program is one of the quickest and most permanent answers to our distressed area problems.

I appreciate your fine support.

Most sincerely,

David L. Francis

David L. Francis, Mayor
City of Huntington

DLF/nn
Enc. 2

Article Title: Prime The Pump Or Train The Individual; Which Is The Better Road To Recovery?

Journal Title: Charleston Daily Mail

Date: March 13, 1961

March 17, 1961.

Dear Mr. Booth:

How nice of you to send me the editorial from the Roanoke Times. You were kind enough to suggest that I not acknowledge it but it is a pleasure to recall my visit in Lynchburg and I do hope you will give Jim Caskie my regards when you see him.

Cordially yours,

Wm. McC. Martin, Jr.

Mr. Lea Booth,
203 Courtland Building,
Lynchburg, Virginia.

Mr. Molony

LEA BOOTH
203 COURTLAND BUILDING
LYNCHBURG, VIRGINIA

March 14, 1961

M

Dear Mr. Martin:

The enclosed editorial reminded me once again of the delightful, informative talk you presented to our Sphex Club in Lynchburg last year. I thought you would like to see this editor's comments.

I should be embarrassed if you bothered to acknowledge this, so please don't consume your valuable time on amenities. I know you need all the time you can find to hold the line against the "new frontier" socialists who disdain the integrity of the dollar you're trying to protect.

Sincerely,

Lea Booth

LB:ew
Enclosure.

The Honorable William McChesney Martin, Jr.
Chairman of the Board of Governors
Federal Reserve System
Constitution Avenue between 20th & 21st, N.W.
Washington, D. C.

Article Title: Recession Cure: Two Views

Journal Title: Roanoke Times (Roanoke, VA)

Date: March 12, 1961

Mr. Shay
Mr. Thomas

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JOHN S. FORSYTHE, GENERAL COUNSEL

United States Senate

COMMITTEE ON
LABOR AND PUBLIC WELFARE

March 16, 1961

The Honorable Wm. McC. Martin, Jr.
Chairman
Board of Governors of the Federal Reserve System
Washington 25, D. C.

Dear Mr. Martin:

Thank you for your letter of March 9th with which you enclosed the 47th annual report of the Board of Governors of the Federal Reserve System.

I found the report most interesting and I am maintaining it in my permanent file.

Your testimony before the Joint Economic Committee was indeed stimulating.

Warm regards.

Sincerely,

Claiborne Pell

Miss Muehlhaus

March 14, 1961

Mr. Joseph A. Livingston
The Evening Bulletin
Philadelphia, Pa.

Your Sunday column re unemployment does a neat job of posing the question: "Do we treat the symptoms -- the unemployment -- the disease, or both?

On Mr. Martin's testimony, however, I suspect your column had to be written before you had a chance to see his text, and when you had only second-hand accounts to go on.

Hence I'm enclosing a copy of his text. As you will see, he did not attempt to measure the quantity of cyclical or structural employment, but simply took (and still takes) the position that we're faced with both and that it is necessary to combat both by actions to get at the differing causes of both.

Best regards.

(Signed) Chas. Molony

Charles Molony,
Assistant to the Board.

Enclosure
CM:nk
cc: Miss muehlhaus

FOR FILES
N. B. Kelly

March 13, 1961.

Dear Will:

Thank you very much for sending me the editorial from the Mamaroneck Daily Times. I am glad to have this and appreciate your taking the trouble to forward it.

These are difficult times indeed and we will have to work things out in a realistic manner.

With all good wishes,

Cordially yours,

Wm. McC. Martin, Jr.

Mr. Will Scholle,
1210 Greacen Point Road,
Mamaroneck, New York.

1210 Greacen Point Road
Mamaroneck, New York

Mch 11-61

Dear Bill,

Attached is a very significant editorial from our local paper "The Mamaroneck Daily Times" which puts credit where it is due. More power to you!

Very sincerely,

Will Scholle

William McChesney Martin
Chairman, The Federal Reserve Board,
Washington, D.C

Article Title: A Different Look at Unemployment

Journal Title: The Daily Times (Namaroneck, N.J.)

Date: March 9, 1961

March 13, 1961.

Dear Ben:

Thank you for your nice letter of March 8 with respect to my testimony before the Joint Economic Committee. I am glad you approve and I am forwarding a copy so that you can browse through it at leisure.

The comments you make are very pertinent indeed and I am in full agreement with them. These are difficult times and we will all have to think through our many problems carefully. In the economic field we are certainly much closer to normal than we have been for a long time.

My best, as always.

Cordially yours,

Wm. McC. Martin, Jr.

Enclosure

Mr. Benjamin Strong,
Chairman of the Board,
United States Trust Company of New York,
45 Wall Street,
New York 5, New York.

United States Trust Company
of New York

45 WALL STREET • NEW YORK 5, N. Y.

HAnover 2-4600

BENJAMIN STRONG
CHAIRMAN OF THE BOARD

March 8, 1961

Dear Bill:

Congratulations on your testimony yesterday! You not only spoke the truth, but nailed-down the fact that the Federal Reserve System is still an independent outfit.

I heartily agree that the measures proposed by the Kennedy Administration can have only minimal effect on the economy. Even then, its limited value may be erased entirely by the psychological effect of the bearish statements coming from all facets of the Government. There seems to be little understanding of the fact that at this stage of our economy, the buying public can very easily be dissuaded from purchasing or expanding their style of living.

For some time I have had the feeling that we are back to normal after a period of approximately thirty years. The first fifteen years covered roughly the Depression and World War, II, when our economy slipped back badly in keeping up with both the population and the normal expansion requirements of our people. From 1945 to 1960, the second fifteen years, we feverishly worked to catch up with what we had lost in the previous fifteen years. This included expansion in this country, as well as bringing other industrial countries back into production. The end of this era coincided with the end of the Eisenhower Administration, which provided such a favorable climate for the tremendous boom of these past fifteen years.

Now the pipelines are filled -- productive capacity has gone too far in many directions -- Europe and other producing countries are back in world markets with brand new plants, low labor costs and high quality. In my opinion, the normal influences on our economy and our markets will again prevail after being pushed aside by the tremendous force of the post-war boom. These include international tensions, consumer psychology, over-production and other unfavorable aspects in certain industries, etc., etc. This, to me, is in fact a return to normal conditions under our type of free enterprise system.

The unemployment problem that you dealt with yesterday so wisely is our biggest difficulty now and in the future. I have thought for a long time that industry must eventually adopt some form of annual wage policy, even though the cost comes out of the stockholders. It is completely inconsistent that we spend vast sums on Social Security, old age pensions, medical benefits, etc., etc., and then offhand lay-off 20,000 men in one day, as the motor industry has just done.

United States Trust Company
of New York

Furthermore, the people in these times will not stand for such treatment. Full annual employment has been successful in a great many industries, including banking, insurance, as well as many manufacturing operations. Its extension broadly to industry would, I feel, have some valuable effect on the economy in general.

It would be a pleasure to chat with you about these matters some time when we can get together. I have no immediate plans for a visit to Washington, but could arrange to run down if the opportunity arises. If you are ever in New York, I hope you will give me the pleasure of entertaining you for lunch here at the Bank. We would also like to show you our new quarters.

Keep up the good work and more power to you! With best regards,

Sincerely,

Ben

Mr. William McC. Martin, Jr., Chairman
Board of Governors
The Federal Reserve System
Washington, D. C.

March 13, 1961.

Dear Mr. Neisser:

Thank you for your nice letter of March 8 and I am glad you give qualified agreement to my testimony before the Joint Economic Committee. I am forwarding a copy of my statement which you may care to peruse.

I was sorry you overlooked enclosing the reprint of your comments mentioned in your letter to me and if you have another copy I would be glad to have them.

Cordially yours,

Wm. McC. Martin, Jr.

Mr. Hans Neisser,
Graduate Faculty of Political and Social Science,
New School for Social Research,
66 West Twelfth Street,
New York 11, New York.

NEW SCHOOL FOR SOCIAL RESEARCH
GRADUATE FACULTY OF POLITICAL AND SOCIAL SCIENCE
66 West Twelfth Street, New York 11, New York ORegon 5-2700
11 Park Ave., Greenvale, N.Y.

3/8/61

Mr.Wm.McC.Martin
Chairman
Board of Governore of the Federal Reserve System
Washington D.C.

Dear Mr.Martin,

since I permitted myself some critical comments on Federal Reserve Policy in a recent Symposion published in the Review of Economic and Statistics, I think it appropriate to express my(qualified) agreement with your statement as reproduced by the New York Times of to-day.Without doubt we have a substantial" structural" or"technological" unemployment; and this cannot be cured by Budget and monetary policies alone; re-training, increasing the mobility of labor is required, too.

A qualification seems to me necessary for steel workers(possibly also auto workers)The unemployment there seems to be less caused by labor saving devices but by a fall in demand;and an increase in armament orders would cure that. More generally, it would not help re-training workers for other industries unless there is additional demand for the products of these industries;and I doubt that without any fiscal and monetary expansion enough of that would materialize. How to bring about this expansion without at the same time discouraging private investment, is a question about which I have thought much, but with which I do not want to bother you.

Yours very sincerely

Hans Neisser

Hans Neisser

P.S.I take leave to enclose
a reprint of my contribution
mentioned above.

March 13, 1961.

Dear Mr. Thorn:

Thank you for your nice letter of March 8 and I am glad that you thought my testimony before the Joint Economic Committee was all right. I am enclosing a copy of the full text for your information and want to thank you for your letter.

Sincerely yours,

Wm. McC. Martin, Jr.

Enclosure

Mr. Marvin D. Thorn,
14 Williams Lane,
Berwyn, Pennsylvania.

MARVIN D. THORN

14 WILLIAMS LANE
BERWYN, PENNSYLVANIA

3/8/61

Dear Mr Martin,

Good for you speaking-up, as I read on front page of today's NY Times.

We need more of this in times like we've experienced in weeks since election.

As a Columbia man, I still think there are too many Harvards in Washington, D.C. !!!

All of us need some solid thinking in the months ahead and you can be a good spokesman

Marvin Thorn

March 13, 1961.

Dear Dick:

Thank you for your nice note of March 8 and I am glad you approved of my testimony before the Joint Economic Committee.

These are difficult times and we have two conflicting philosophies to deal with. Perhaps neither one of them is entirely correct and the middle ground will come closer to the truth. In any event, we are going to have our difficulties. I am confident, however, we can solve them.

My best, as always.

Cordially yours,

Wm. McC. Martin, Jr.

Mr. C. Richard Youngdahl,
20 Broad Street,
New York 5, New York.

C. RICHARD YOUNGDAHL
TWENTY BROAD STREET
NEW YORK 5, N.Y.

March 8, 1961

Dear Bill:

Your testimony before the Joint Committee yesterday was a real breath of fresh air, after testimony and speeches by the New Frontier's impractical and naive general theorists.

My Harvard, Yale and Minnesota academic friends are preoccupied with "lever-pulling" to cure basic structural problems, and this has me greatly worried. I have heard them speak of a $35 to $40 billion "income gap" with a combination of annoyance, sorrow, and a nervous twitching in my stomach. They speak of 1959 as falling short of our "potential" by some massive amount in income without, apparently, any ability to recall the frantic pace of activity at the time and the degree to which people then were becoming convinced that inflation was a present and a future certainty. If we could not activate the "fanny-sitters" in West Virginia with the tempo of business as it was in 1959, how can we hope to burn the fires of the economy brightly enough in '62 or '63 to pull these people into the stream of employment? Your testimony on retraining and resettlement got to the heart of the problem, and it was good to read of it.

It is not necessary for me to comment to you personally about the recent developments in Fed open market policy. I believe I know your views well enough to assume that this change was a strategic retreat on a secondary, albeit a highly important, point in order to be in a better position to defend the key point -- that is, flexible monetary policy itself.

Best regards.

Sincerely,

Dick

CRY:ho

Mr. William McC. Martin, Jr.
Chairman
Board of Governors
Federal Reserve System
Washington 25, D. C.

March 13, 1961.

Dear George:

Thank you for your letter of March 9 and I am glad you approved of my testimony. I am forwarding a copy of the full text.

It was good to have a visit with you and I hope our paths will cross again before too long.

Cordially yours,

Wm. McC. Martin, Jr.

Enclosure

Mr. George Soloveytchik,
c/o Great Northern Hotel,
118 West 57th Street,
New York, 19, New York.

George Soloveytchik March 9, 1961

GREAT NORTHERN HOTEL

COCKTAIL LOUNGE • RESTAURANT • GRILL

118 WEST 57th STREET, NEW YORK 19, N. Y.

CABLE ADDRESS "NORTHHOTEL" Telephone CIRCLE 7-1900

Mr. William McChesney Martin, Jr.
Chairman of the Board of Governors
of the Federal Reserve Board
Washington, D.C.

Dear Bill:

Just a few lines to say how delighted I am to see that you have spoken out once more and that you have stated in such emphatic terms that chronic unemployment cannot be cured by inflationary policies.

Well done! And I hope that you will stick to your guns and repeat this obvious truth again and again, even though the powers that be do not seem to recognize it.

It was nice to have a long visit with you, and the only thing I regret is that we agree on everything. It would have cheered me up no end if you had been able to prove to me that I was wrong in my assessment of the situation, and that the confidence crisis was not as serious as I think. At the same time, I was glad to have this additional proof that you and I seem to see the situation from much the same sort of angle, even if at times it is a most worrying one. Personally, I still think that -- despite everything -- circumstances demand dearer and <u>not</u> cheaper money. However, you know best. Unfortunately, I did not have an opportunity, this time, of meeting either Dillon or Roosa, but hope to do so on some other occasion.

With warmest personal greetings, and hoping to see you next year, I am,

Yours as ever,

George

George Soloveytchik

GS:ilp

P.S. I shall be leaving for Europe on March 24th

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

3/8

Mr. Martin--

This is for your information only. Mr. Molony said "of course" and I sent the copy on with the attached note from me.

Mr. French said he hopes to get to Washington sometime and would enjoy an opportunity of visiting with you.

mnm

March 8, 1961.

Mr. Vincent Martire,
Tax Foundation Inc.,
30 Rockefeller Plaza,
New York, New York.

Dear Mr. Martire:

In Mr. Martin's absence from the office, Mr. Robert French spoke to me today with respect to reproducing in whole, or in part, Mr. Martin's testimony of yesterday before the Joint Economic Committee.

Mr. Martin would, I know, be very pleased to have you use his statement in your publication and at Mr. French's suggestion I am sending a copy directly to you.

Sincerely yours,

(Miss) Margaret Muehlhaus,
Secretary to Mr. Martin.

Enclosure

March 8

Mr. Molony--

After Mr. Martin had left this morning, Mr. Robert French of the Tax Foundation in New York City phoned him--and talked to me.

Mr. French knows Mr. Martin (was Dean of the Business School at Tulane at the time Mr. Martin got his honorary degree) and therefore wanted to call him personally.

The publication of the tax foundation often uses statements of men in public office in their monthly issues-- Mr. French has seen the newspaper reports of Mr. Martin's statement yesterday before the Joint Economic Committee and wanted permission to use it in the next issue. They may shorten it a bit (for they have space limitations) but the statement would be identified.

I told Mr. French that it was a public document and I was sure there would be no objection to their reproducing it; however, that I would check it with you.

Mr. French asked me to send a copy today to Mr. Vincent Martire at the Tax Foundation, 30 Rockefeller Plaza, with a note saying they could use it.

Mr. French suggested that if there were any questions you might want to talk to their representative in the Washington Office--Mr. Waterfield--or Mr. Martire in New York, at Circle 7-3690.

May I send it?

Thanks

mnm

March 8, 1961.

The Honorable Paul H. Douglas,
Vice Chairman,
Joint Economic Committee,
Congress of the United States,
Washington 25, D.C.

Dear Senator Douglas:

In reply to your letter of March 2, 1961, please be assured that steps are actively in process looking toward the publication of current statistics on the Government securities market. As I indicated in response to your questions at yesterday's hearing, no specific date has been fixed for the initial publication of these data. However, it is anticipated that the program will be put on a public reporting basis some time this Spring, probably by the first of April.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

cc: Mr. Young
Mr. Shay
Miss Muehlhaus

KAK:RAY:JWS:mnm

March 8, 1961.

The Honorable Wright Patman,
Chairman, Joint Economic Committee,
Congress of the United States,
Washington 25, D.C.

Dear Mr. Chairman:

In reply to your letter of March 2, 1961, please be assured that steps are actively in process looking toward the publication of current statistics on the Government securities market. As I indicated in response to questions by Senator Douglas at yesterday's hearing, no specific date has been fixed for the initial publication of these data. However, it is anticipated that the program will be put on a public reporting basis some time this Spring, probably by the first of April.

Sincerely yours,

(Signed) Wm. McC. Martin, Jr.

Wm. McC. Martin, Jr.

cc: Mr. Young
Mr. Shay
Miss Muehlhaus

KAK:RAY:JWS:mnm

March 20, 1961

To Chairman Martin Subject: Samuelson's testimony re unemployment.

From Jerome W. Shay

This afternoon, Dr. Paul Samuelson testified before the Holland Subcommittee on Unemployment and Automation of the House Committee on Education and Labor. Dr. Samuelson, who explained that he was speaking purely as a private citizen, had no prepared statement.

Before submitting himself to questioning by members of the Subcommittee, Dr. Samuelson spoke briefly on various aspects of unemployment. During these opening remarks, he referred to your appearance and that of the Council of Economic Advisers recently before the Joint Economic Committee and the views there expressed with respect to "structural" and "cyclical" unemployment. Dr. Samuelson's first remark with respect to this testimony was that there was only a difference of emphasis and that it was a healthful thing to have the matter discussed as it was. He then went on to say that "structural" or "hard-core" unemployment cannot be remotely affected by monetary or fiscal policy, since such unemployment calls for special measures providing for retraining of labor, mobility of labor, et cetera. He added, however, that the rate of effectiveness of any such special measures would be affected by fiscal and monetary policy. By way of explanation, he added that, when we are in a period of high demand, the sustained pull of job opportunities accompanying the high demand tends to draw off excess labor from one area into another area or activity. Thus, he seemed to conclude that "structural" unemployment is not a malady completely separate from the question of over-all demand, which is affected, he said, by monetary and fiscal policy.

As previously indicated, these remarks were initiated by Dr. Samuelson and were not in reply to any questions from members of the Subcommittee, none of whom, during the course of the hearing, referred to your testimony or that of the Council earlier this month.

Later, during the hearing, Dr. Samuelson made a further reference to your testimony and that of the Council by saying that "when all the fireworks are over there will be a great deal of agreement between Mr. Martin and Mr. Heller," although there will be, he added, a "residual amount of disagreement" of the kind that one should expect between persons of not identical interests or backgrounds, such as almost any two economists. In answer to a question as to what the percentage of unemployment might be at the peak of the next recovery, Dr. Samuelson said that a reduction of unemployment to four per cent might not be too much to hope for, but that it would depend on how successful we are with monetary and fiscal policy. At a later point, he went on to say that unless fiscal and monetary policy does its job very well, there will be more and more agitation for the institution of a shorter work week, in order to cut down the continuing high unemployment.

cc: Each Board Member
Messrs. Thomas, Young, Molony, Fauver, Knipe, Ford, Alderfer, Sherman, Noyes, Marget, and Wernick

JM

March 6, 1961

To Chairman Martin

From Jerome W. Shay

Subject: CEA testimony before Joint Economic Committee

This morning Walter Heller, accompanied by Kermit Gordon and James Tobin, testified before the Joint Economic Committee. They have agreed to appear again before the Committee at a date as yet undetermined for further questioning by members of the Committee, inasmuch as it was agreed that the substantial length of the prepared testimony presented this morning gave Committee members insufficient opportunity to prepare themselves.

While there was good attendance by Committee members, the spirit of the questioning was very moderate and there were no questions at all with respect to the Federal Reserve or to monetary policy. As a matter of fact, the only Committee member to mention monetary policy was Congressman Reuss, who expressed pleasure in seeing that the Council "had reinstituted the practice of making recommendations with respect to monetary policy."

The main statements on monetary policy in the Council's statement are as follows:

"Monetary Policy and Debt Management

"In this recession, for the first time since 1931-32, expansionary monetary policy has been limited by the international financial position of the United States. Over the past six months our balance of payments deficit has been severely aggravated by the outflow of short-term capital attracted by higher short-term interest rates abroad. To stem the outflow, Federal Reserve authorities have had to limit expansion of money and credit, especially in recent months, to keep short-term interest rates from falling too far. Short-term rates have remained 1.5 to 2 percentage points above past recession levels. The Federal Reserve discount rate, which fell as low as 1.75 percent in the 1958 recession, is 3 percent today. The Treasury bill rate reached 0.6 percent in May 1958 but stands at 2.6 percent today, up from its recent low of 2.1 percent in November 1960.

"The Federal Reserve has sought since October to expand bank reserves in ways that do not directly lower bill rates and other rates important in holding internationally mobile liquid funds. These efforts have met with some success. The money supply (defined conventionally as demand deposits and currency) has risen 1.4 percent since June 1960, and the money supply (defined to include also time deposits) has risen about 4 percent. However, interest rates have remained relatively high throughout all segments of the money and capital markets. Whether interest rates are regarded as a cause or as a symptom of borrowing and lending activity, substantial monetary and credit expansion can scarcely occur without significant easing of rates.

"The 'prime rate'--the rate New York banks charge their prime-risk customers for commercial loans--is 4.5 percent now, in comparison with 3.5 percent in 1958 and 3 percent in 1954. Corporate Aaa bonds yield 4.2 percent now, in comparison with 3.6 percent and 2.8 percent in the two preceding cyclical troughs. Table 5 compares interest rate levels today with those in previous recessions, and shows in the same comparative perspective how little long-term interest rates have fallen so far in this recession.

"The Federal Reserve has recently announced that it is purchasing long-term U. S. Government securities on the open market. The new policy is an extension of its efforts to provide additional reserves by purchases that do not directly depress the short-term rate. The objective is to lower long-term interest rates, in order to increase business investment and residential construction, while maintaining the discount rate and related short-term rates at internationally competitive levels. Treasury public debt operations are also geared to this objective. Federal Reserve and Treasury operations may be expected to result in reduction of the stock of long-term bonds available to private investors, relative to the outstanding supplies of short securities. The extent to which the maturity structure of rates can be 'twisted' by these operations remains to be seen. But the experiment must be tried. The domestic economy urgently needs the stimulus of lower effective long-term and commercial rates. At the same time, as confidence in the dollar is restored and as interest rates abroad continue to fall, the constraint on our short-term rate can safely be relaxed."

It should be noted also that, in connection with housing credit, the Council's statement observed that "Further measures to stimulate housing demand will become possible as general monetary conditions are further eased." And, in a general context, the statement observed that "the move to reduce interest rates and increase credit availability" can have important stimulative effects on the economy.

A point emphasized in the prepared statement of the Council and also in the course of questioning was that an economic upturn would be "only the beginning, not the end, of the solution of our economic problems." This was given further meaning by the emphasis placed on the fact that any lag in the taking effect in the economy of increased Government spending would not have detrimental effects because of the unusual amount of sluggishness in the economy quite aside from the present recession. This would suggest that the Council feels that any measures to stimulate the economy now probably should be continued well into the recovery stage, and longer.

The Council, apparently, feels that the recession has reached its low point, although as to possible signs of upturn they were rather vague, and indicated, as President Kennedy has, that a renewed look at the entire situation would be taken in April.

With respect to its own organization, the Council clearly feels that it needs more staff to do its job properly. Mr. Heller indicated that this would mean employing at least 20 trained economists rather than the present 11.

Copy of Council's statement attached hereto.

Attachment
cc: Each Board Member
Messrs. Thomas, Young, Molony, Fauver, Knipe, Ford, Alderfer, Sherman, Noyes, and Marget

March 3, 1961

Chairman Martin:

The attached letter has been discussed with Ralph Young. As the subject of the letter will come up for approval at the meeting of the Open Market Committee on Tuesday morning, you may wish to indicate the result of the meeting to Senator Douglas, if possible, before you testify on Tuesday afternoon and, thus, leave to him the decision whether or not to raise the matter during the hearing.

It is our understanding that the letter was written--perhaps primarily--to add weight on the side of favoring the reporting system.

JWS

Attachment

WRIGHT PATMAN, TEX., CHAIRMAN
RICHARD BOLLING, MO.
HALE BOGGS, LA.
HENRY S. REUSS, WIS.
MARTHA W. GRIFFITHS, MICH.
THOMAS B. CURTIS, MO.
CLARENCE E. KILBURN, N.Y.
WILLIAM B. WIDNALL, N.J.

WM. SUMMERS JOHNSON,
EXECUTIVE DIRECTOR

PAUL H. DOUGLAS, ILL., VICE CHAIRMAN
JOHN SPARKMAN, ALA.
J. W. FULBRIGHT, ARK.
WILLIAM PROXMIRE, WIS.
CLAIBORNE PELL, R.I.
PRESCOTT BUSH, CONN.
JOHN MARSHALL BUTLER, MD.
JACOB K. JAVITS, N.Y.

JOHN W. LEHMAN, DEPUTY EXECUTIVE
DIRECTOR AND CLERK

Congress of the United States

JOINT ECONOMIC COMMITTEE

(CREATED PURSUANT TO SEC. 5(a) OF PUBLIC LAW 304, 79TH CONGRESS)

March 2, 1961

The Honorable Wm. McChesney Martin
Chairman
Board of Governors of the
Federal Reserve System
Washington 25, D. C.

Dear Mr. Martin:

During the 1959 hearings of the Joint Economic Committee in connection with its study of Employment, Growth, and Price Levels, we learned that the Federal Reserve System had established in the Federal Reserve Bank of New York a statistical section devoted to developing, in cooperation with the Treasury and the dealers, a regular reporting system on volume, positions, financing and prices in the market for Federal Government securities. We were pleased with this action in line with our views on the importance of regular reporting of the facts about this market. So far, a public reporting system has not resulted from this program. We have not inquired officially about progress though Mr. James W. Knowles of the Committee staff has been in regular communication with the technicians working on the problem.

The lapse of a year and a half has not diminished my interest in this problem nor eroded my belief that the establishment of a reporting system for the market in Federal Government securities is essential to the success of both monetary and debt management policies. I hope that it will be possible for this program to soon be put into operation.

Faithfully yours,

Paul H. Douglas

Paul H. Douglas
Vice Chairman

WRIGHT PATMAN, TEX., CHAIRMAN
RICHARD BOLLING, MO.
HALE BOGGS, LA.
HENRY S. REUSS, WIS.
MARTHA W. GRIFFITHS, MICH.
THOMAS B. CURTIS, MO.
CLARENCE E. KILBURN, N.Y.
WILLIAM B. WIDNALL, N.J.

WM. SUMMERS JOHNSON,
EXECUTIVE DIRECTOR

Congress of the United States

JOINT ECONOMIC COMMITTEE

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PRESCOTT BUSH, CONN.
JOHN MARSHALL BUTLER, MD.
JACOB K. JAVITS, N.Y.

JOHN W. LEHMAN, DEPUTY EXECUTIVE
DIRECTOR AND CLERK

March 2, 1961

The Honorable Wm. McChesney Martin
Chairman
Board of Governors of the
Federal Reserve System
Washington 25, D. C.

Dear Mr. Martin:

The Joint Economic Committee was pleased to learn in 1959 that the Federal Reserve System had established at the Federal Reserve Bank of New York a statistical section devoted to developing a reporting system for Federal Government securities which would cover volume, positions, financing and prices. It was our understanding that this system would be developed in cooperation with the Treasury and the dealers operating in the market for Federal Government securities.

Although we have not as yet received word of the beginning of regular public reporting as a result of this effort, our interest in seeing that this program is put into operation has not diminished. Mr. James W. Knowles of the committee staff has acted for us in maintaining regular communication with the technicians working on this program. It is important, I believe, that this program be put on a regular public reporting basis as soon as possible in view of the technical problems involved. I hope that you can offer assurance that public reporting can begin within the near future.

Sincerely yours,

Wright Patman

Wright Patman
Chairman

Article Title: Martin Expects -Some Success- In New Reserve Board Market Policy

Journal Title: Dow Jones News Wire

Date: March 1961

ALLAN SPROUL
KENTFIELD, CALIFORNIA

March 14, 1961.

Dear Bill:

Thank you for sending me a copy of your recent statement before the Joint Economic Committee. It was given prominence in the local press but, as is often the case with our papers when reporting on national or international affairs, the account was truncated and garbled.

I think you were right to try to put the present situation in perspective by outlining the relevant past. If I would have written your capsule history a little differently, it would be because every man has his own point of view concerning the drama in which he played a part.

Now, the System is in the cross-fire of those who see what it has done as hauling down the flag of "independence", and those who hope for or expect a return to "pegging" or something like it. Critics and embarrassing allies must be shown to be equally wrong.

My word of counsel would be to avoid emphasis on the temporary character of the recent action of the Federal Open Market Committee, which is the tack which some defenders of the faith seem to have taken. Quite apart from the merits or demerits of the technique of "bills only" or "bills preferably", I consider the "rules of the game" an unneccessary and undesirable hindrance to appropriate flexibility in general policy and in techniques. It should not be necessary, again, to make every change in technique appear to be a major policy decision. I would avoid painting myself into that corner once more.

I liked what you had to say about structural defects in the economy, and about the impossibility of offsetting all of them by way of monetary policy or monetary-fiscal policy. This is a most difficult area in politics and in economics, and it has been mostly shunned by politicians and largely shunned by economists. You probably noticed that, in the report which my associates and I prepared for the President, we spoke of over-burdening monetary policy in opposing economic trends having there roots in structural developments. (That report was a tour de force, prepared in tendays, with a space limit of twenty five pages, by three men working together for the first time. I am glad you found it valuable.)

For myself, I have no doubt that the System will continue to meet its problems effectively, so long as its general constitution and organization are not tampered with by those who would force it into a new and different mold, and so long as the quality of its personnel is maintained. It has the virtues and strengths of a political invention which, by natural growth and development, has adapted to our political and economic environment.

With best regards.

Sincerely,

Allan Sproul.

P. S. Your phrase, "leaning against the wind", has become a part of our economic lexicon. I doubt if "leaning against cross-winds -- simultaneously" has the same quality!

A. S.

Airmail

March 7, 1961.

Dear Allan:

Since I took your name in vain in my testimony before the Joint Economic Committee, I wanted to get the full text to you promply.

All of us here have read with great interest the Task Force report you made to the President and appreciate all the work you have done.

We are continuing to struggle with our many problems and hope we can resolve some of them.

With all good wishes,

Cordially yours,

Wm. McC. Martin, Jr.

Enclosure

Mr. Allan Sproul,
Box 365,
Kentfield, California.

March 7, 1961.

Walter--

I thought you and your associates might want to have copies of my statement to the Joint Economic Committee today.

WMM

Enclosures 3

(To Chairman Heller of the ~~Joint Economic Rep~~ Council of Economic Advisers)

One copy each sent by messenger to

Secretary Dillon, Under Secretary Roosa, and Under Secretary Fowler of the Treasury

and David Bell, Director of the Bureau of the Budget

March 7, 1961.

Dear Walter:

Thanks for sending over the copies of your statement yesterday before the Joint Economic Report. It was helpful to get them so promptly and we appreciate it.

With all good wishes,

Cordially yours,

Wm. McC. Martin, Jr.

The Honorable Walter W. Heller,
Chairman,
Council of Economic Advisers,
Washington 25, D.C.

3/2

Note:

Mr. Shay advises Mr. Martin still scheduled to appear before Joint Economic Committee on Tuesday afternoon at 2:30.

Secretary Dillon will appear that morning.

David Bell has "begged off" for Monday afternoon, the 7th; and Hitch of Defense Dept. is off for Wednesday morning, the 9th.

Heller will go on Monday morning, as scheduled.

mnm

THE CHAIRMAN OF THE
COUNCIL OF ECONOMIC ADVISERS
WASHINGTON

February 28, 1961

MEMORANDUM FOR MR. MYER FELDMAN

From : Walter W. Heller W.

Subject: March 6th Hearing

After checking with the President, we have decided to go ahead with the March 6th date on the JEC hearing, in spite of some discomfort occasioned by the delay of the budget message. The Committee interprets this to mean that David Bell and Charlie Hitch will be heard later, with the other witnesses appearing next week.

Copies to:
Secretary Dillon
Chairman Martin
Director Bell
Asst. Secretary Hitch
Wm. Johnson, JEC

Lehman -- 5171

FOR IMMEDIATE RELEASE
February 13, 1961

CONGRESS OF THE UNITED STATES
JOINT ECONOMIC COMMITTEE

Chairman Patman Announces Re-scheduling
of Hearings on the President's Economic Report
and the Economic Situation and Outlook

Representative Wright Patman (D., Texas), Chairman of the Joint Economic Committee, said today that the government witnesses previously announced as appearing before the Joint Economic Committee on February 20, 21, and 22 have, by mutual agreement, been re-scheduled for March 6, 7 and 8. The new schedule will permit more time for the preparation of additional material by the incoming administration.

The hearings which are being held on the President's Economic Report and the current economic situation began last Thursday and Friday when a panel of technical experts and representatives of labor, management, farm and other organizations were heard. A copy of the revised hearing schedule is attached.

1961-4

REVISED SCHEDULE OF HEARINGS
ON THE 1961 ECONOMIC REPORT OF THE PRESIDENT
AND THE ECONOMIC SITUATION AND OUTLOOK

(All hearings are open to the public)

Monday, March 6, 10:00 a.m. -- Room 318, Old Senate Office Bldg.

Council of Economic Advisers

WALTER W. HELLER, Chairman
JAMES TOBIN
KERMIT GORDON

Monday, March 6, 2:00 p.m. -- Room 318, Old Senate Office Bldg.

DAVID E. BELL
Director
Bureau of the Budget

Tuesday, March 7, 10:00 a.m. -- Old Supreme Court Chamber
Senate Wing, U. S. Capitol

C. DOUGLAS DILLON
Secretary of the Treasury

Tuesday, March 7, 2:~~00~~ 30 p.m. -- Old Supreme Court Chamber
Senate Wing, U. S. Capitol

WILLIAM McCHESNEY MARTIN
Chairman
Board of Governors, Federal Reserve System

Wednesday, March 8, 10:00 a.m. -- Old Supreme Court Chamber
Senate Wing, U. S. Capitol

CHARLES J. HITCH
Assistant Secretary of Defense (Comptroller)
Department of Defense

February 13, 1961.

Dear Walter:

Thank you for sending me a copy of your letter of February 10 to Mr. Patman in which I am glad to see you speak for me also. I think this will be a better arrangement.

With all good wishes,

Cordially yours,

(Signed) Bill

Wm. McC. Martin, Jr.

The Honorable Walter W. Heller,
Chairman,
Council of Economic Advisers,
Washington 25, D.C.

cc: Mr. Shay

WMM:mnm

THE CHAIRMAN OF THE
COUNCIL OF ECONOMIC ADVISERS
WASHINGTON

February 10, 1961

Honorable Wright Patman, Chairman
Joint Economic Committee
Congress of the United States
Washington, D. C.

Dear Mr. Patman:

We greatly appreciate your willingness to accommodate the desire of Administration witnesses to postpone their appearances before your Committee. We should like to effect a two weeks' postponement, and it is our understanding that this change will have the approval of your Committee.

This would provide the additional time needed for preparation of testimony and would also have the important advantage of holding the hearings after the President's message concerning budget and fiscal revision has been forwarded to the Congress.

This postponement is also welcomed by Director Bell, Secretary Dillon, and Assistant Secretary Hitch, who have asked me to indicate their endorsement and appreciation of this change. Informally, I also had an opportunity to mention the probable postponement to Chairman Martin.

We regret the inconvenience we may have caused the Committee and the staff, and we wish again to express our debt to you for so graciously arranging the postponement.

Sincerely yours,

Walter W. Heller

Copies to:
Director Bell
Secretary Dillon
Assistant Secretary Hitch
Chairman Martin
Mr. Feldman
Mr. O'Brien

February 10, 1961

To Chairman Martin

From Jerome W. Shay

Subject: Joint Economic Committee Hearings

This morning the Joint Economic Committee concluded the first part of its hearings on the President's economic report. The first part of the hearings has been devoted to non-Government witnesses.

This will confirm that the witnesses for the Government, including yourself, will be heard by the Committee sometime during the week of March 6, so that the present schedule for Government witnesses for the week of February 20 is no longer effective. This was announced officially this morning by Chairman Patman. Specific dates for appearances will be worked out later.

One of the witnesses this morning was Herbert Stein, Research Director for the CED, whose testimony dealt largely with the relationship between tax rates, Governmental expenditure programs and unemployment. After stating that throughout the period 1955-59 there was a relationship between tax rates and Government expenditures that balanced the budget when unemployment was 5.2 per cent, Mr. Stein related that in the first half of 1960 we moved to a surplus far greater than would have been yielded by this 1955-59 relationship. In the second half of 1960, he added, we remained far above the previous relationship, getting a surplus of $1.2 billion with 6.1 per cent unemployed. It was his belief that the weight of the 1960 relationship between surplus and unemployment contributed to stopping the recovery that was under way in 1959. Among other things, he added:

> "The attempt to achieve high employment in the face of a budget that would yield very large surpluses at high employment requires rapid monetary expansion to offset the depressing effect of the budget. This means low interest rates, and unless other countries are following a similar policy, this is likely to cause an outflow of capital and balance of payments difficulties.
>
> "In fact, during 1960 we did get an easing of monetary policy. This was not sufficient to maintain high employment, but it did contribute to the decline of U. S. interest rates, to the outflow of short term capital and to the balance of payments deficit."

The other witnesses this morning were W. E. Hamilton, American Farm Bureau Federation; Angus McDonald, National Farmers Union; Herschel D. Newsom, National Grange; and Howard L. Stier, Federal Statistics Users' Conference. Only Hamilton and McDonald made references to monetary policy. Hamilton, in effect, defended the Federal Reserve System's position, while McDonald indicated his view that monetary policy for the past few years "had proven to be fallacious." In discussing this matter with these witnesses, Senator Proxmire's comment was that the relationship between money supply and GNP "had been tighter recently than since Andrew Mellon was Secretary of the Treasury."

It might be interesting to observe that most of the time of the testimony of the witnesses from the farm organizations was spent on possible ways and means of getting vigorous antitrust action against administered prices and other pricing practices alleged to be detrimental to farmers and small businesses.

During the full day and a half of hearings just concluded there has been very little interest demonstrated in Federal Reserve matters by members of the Committee.

cc: Each Board Member
Messrs. Thomas, Young, Molony, Fauver, Knipe, Ford, Alderfer, Sherman, Noyes, and Marget.

February 10, 1961

To Chairman Martin AM Subject: Joint Economic Committee Hearings

From Jerome W. Shay

Yesterday afternoon the Joint Economic Committee continued its hearings by receiving testimony from Walter P. Reuther on behalf of the AFL-CIO; Emerson P. Schmidt, United States Chamber of Commerce; and George G. Hagedorn, National Association of Manufacturers.

Mr. Reuther, in a prolonged statement to the Committee, which presented virtually nothing that was new, left no time for any consequential questioning and little time for the statements by the other two witnesses. Briefly, Mr. Reuther's position, in effect, was that President Kennedy's economic proposals do not go far enough, either as anti-recession measures or as correctives for the long pull. Mr. Reuther's main concern was with automation and the continuing upward trend in unemployment. Perhaps his main proposal was for immediate enactment of discretionary authority in the President to reduce personal income taxes temporarily when necessary to stimulate the economy.

With respect to monetary policy and the Federal Reserve, Mr. Reuther said:

> "We welcome the President's announcement that measures are already under way to increase the flow of funds at declining long-term interest rates. While, in view of the outflow of gold, short-term interest rates must for the time being be maintained, we should set as our objective, to be achieved as quickly as practicable, a monetary policy conducive to vigorous economic growth. This requires abandonment of the 'bills only' or 'bills usually' policy.
>
> "An adequately expanding money supply at reasonable interest rates is essential to healthy growth. This has been denied the nation in recent years in part because of the unrepresentative character of those who set Federal Reserve policy. The Federal Reserve Act should be amended to provide for adequate representation of consumer, small business and labor interests on the governing and advisory bodies of the Federal Reserve system which is now dominated by the viewpoint of bankers and big business."

A main burden of Emerson Schmidt's testimony was the lack of clarity, thus far, as to what the new Administration's ideas really are. "Obviously," he said, "it is impossible to appraise in any useful way something which is still in the process of being born."

In discussing what he called "The Disappointments of 1960," Mr. Schmidt said that "...the money supply failed to grow; during half of the time in 1960 the money supply ... was below the year-end level in 1956 ... In December 1960 the money supply was $1 billion lower.... than in December 1959."

Mr. Hagedorn, whose statement contained no criticism of monetary policy, said that "the most urgent domestic problem facing the nation is the current rate of unemployment." He said that the two chief economic maladjustments are "the constant tendency toward increasing unit labor costs which places restraints on employment, production, and trade; and a tax system which impedes the accumulation of capital and reduces incentives."

The entire first day of the hearings was marked by a seeming lack of interest on the part of the members of the Committee, even though most of the members were in attendance.

cc: Each Board Member
Messrs. Thomas, Young, Molony, Fauver, Knipe, Ford, Alderfer, Sherman, Noyes, and Marget.

February 9, 1961

To Chairman Martin

From Jerome W. Shay

This morning, the Joint Economic Committee commenced hearings on the Economic Report of the President (the Eisenhower Report) and subsequent economic messages of President Kennedy.

The only points of real significance for the Federal Reserve were raised by Senator Proxmire and Congressman Reuss in connection with the testimony of Roy L. Reierson, of the Bankers Trust Company, who was one of the panel of five witnesses appearing before the Committee this morning

Senator Proxmire asked Mr. Reierson if the Federal Reserve determined interest rates during the '30's and during World War II. Mr. Reierson indicated that, while those periods, of course, were far different from the present period, he felt that the Federal Reserve did have a strong influence on interest rates during World War II but that the interest rates during the '30's were attributable almost entirely to the depressed economy.

Mr. Reuss, in effect, asked Mr. Reierson to comment on a program, whereby the Treasury would issue substantial quantities of long-term obligations--either for cash or in retirement of outstanding obligations--with the Federal Reserve shifting more of its portfolio into long-terms. Mr. Reuss made the suggestion, he explained, because he felt that this would assist in keeping up short-term interest rates and lowering long-term rates and also enable the Treasury somewhat to extend the maturity of the debt. Mr. Reierson's reply was that the main difficulty in this entire matter is the lack of assurance as to what decisions investors would make. His own feeling seemed to be that there is no assurance that this would encourage long-term money to move into mortgages and other private obligations instead of gravitating to short-term obligations, which would only aggravate the situation by tending to depress short-term interest rates without any appreciable effect on long-term rates.

The other members of the panel appearing before the Committee this morning were:

Louis J. Paradiso, Assistant Director-Chief Statistician,
Office of Business Economics, U. S.
Department of Commerce,
Washington, D. C.

George Cline Smith, Vice President-Chief Economist,
F. W. Dodge Corporation,
New York, N. Y.

Ewan Clague, Commissioner,
Bureau of Labor Statistics,
U. S. Department of Labor,
Washington, D. C.

and

George Brandow, College of Agriculture,
Pennsylvania State University,
University Park, Pennsylvania.

Mr. Reierson's statement to the Committee, however, was the only one of any direct consequence with respect to matters concerning Federal Reserve policy. An excerpt from his statement in this connection follows:

"The increased flow of savings and the currently reduced level of economic activity make it reasonable to expect some further easing of bond yields in the months immediately ahead. Short-term rates, however, are not likely to be affected significantly by these downward pressures in view of the demonstrated pull of foreign money markets and the importance of balance of payments considerations for Federal Reserve policy. Moreover, with the economy apparently approaching the bottom of the current contraction, the next few months may well bring signs of an upturn in business and in credit demands. These, together with the large Treasury borrowings already in sight for the second half of this year, suggest that later in 1961 underlying economic forces may well be pointing toward higher interest rates. In fact, it may be pertinent to recall the experience of 1958-59, when a large Treasury deficit compounded the rising credit needs of a business recovery and thus greatly enhanced the upward pressures on interest rates.

"A new factor in the interest rate outlook is the endorsement by the President of a program to attract more funds into the capital markets at lower yields and at the same time to halt further declines in short-term rates in order to curtail the outflow of gold. Presumably, this would involve, on the one hand, Federal Reserve purchases of longer-term Government obligations to reduce bond yields and, on the other hand, sales of shorter-term securities to prevent money market yields from falling. Also, the Treasury would probably be expected to cooperate through reliance upon the issuance of short-term securities.

"Admittedly, to the extent that Federal Reserve purchases of Government bonds induce a shift into mortgages and other long-term investments, a major objective of the program would be met. Essentially, however, the aims are contradictory, as the President's message acknowledges, for as bond yields decline, the inducement to invest at long term will be weakened, and holders of Government bonds may instead prefer to shift into short-term securities until long-term yields become more attractive. This would tend to divert funds from the investment markets and reduce interest rates in the short-term market. The many hazards and complexities involved in this program thus place heavy additional responsibilities upon both the Federal Reserve and the Treasury if constructive results are to be achieved.

"The Federal Reserve, until a business upturn becomes evident, faces the delicate task of following policies conducive to recovery without contributing to a further outflow of short-term funds, and hence of gold, to the higher yielding money markets abroad. However, the task is not insuperable. A moderate rise in short-term rates at home would reduce the attractive of foreign money centers without adversely affecting the business situation at home; bank lending rates are not likely to be raised as a result, nor would such an increase in short-term rates, under present conditions, divert funds from the long-term markets. Furthermore, such a rise in short-term rates need not prevent the Federal Reserve from augmenting the lending power of the commercial banks if the Treasury, in turn, employs debt management policies that complement the aims of the Federal Reserve.

"The Treasury already faces a chronic problem in the continuing shortening of its debt with the passage of time. Added emphasis on the use of short-term securities would further unbalance the maturity structure of the debt and create increasingly difficult refinancing problems for the not too distant future. Financing through long-term bonds, on the other hand, would be criticized as diverting funds from other investment markets at a time when the economy is sagging. A way out of this dilemma may be found by resort to the issuance of Treasury securities in the maturity range suited to commercial bank investment. Such a Treasury policy, complementing the policy of the Federal Reserve, would lead to higher deposits, improved loan-deposit ratios, and increased lending capacity of the commercial banks without depressing money market rates.

"The chances for a successful reconciliation of the conflicting aims of the President's program would be increased if Federal Reserve purchases of longer term Government securities were to be undertaken at times when reserves would ordinarily be provided for credit policy reasons and thus would be substitutes for purchases of Treasury bills. It should be understood that the program is not designed to interfere with flexible credit policy or achieve any particular level of long-term yields. Above all, it should be made unmistakably clear to the market that this is not the first step in a return to pegged interest rates - a prospect which would open the gates to inflationary psychology at home and to renewed attacks on the dollar from abroad.

"The strength of the dollar remains the most important single problem in the monetary field, and goes beyond the matter of interest rates alone. There is some basis for hope that we have seen the worst of the current wave of skepticism: foreigners appear to have gained some assurance from the developments of recent weeks. Ultimately, however, confidence in the dollar can be maintained only if the deficit in our international accounts is eliminated or at least reduced very substantially and if, moreover, we follow domestic policies and practices - in such matters as wages, prices, the budget, debt management and credit - that will stop the persistent erosion of the purchasing power of the dollar and enhance our position in a highly competitive world.

"If we wish to maintain the integrity of the dollar, and if we desire to remain free to use fiscal and credit policies as tools for economic stabilization and growth, we must take to heart President Kennedy's recent words: 'We cannot afford unsound wage and price movements which push up costs, weaken our international competitive position, restrict job opportunities, and jeopardize the health of our domestic economy.'"

cc: Each Board Member
Messrs. Thomas, Young, Molony, Fauver, Knipe, Ford, Alderfer, Sherman, Noyes, and Marget.

CONGRESS OF THE UNITED STATES
JOINT ECONOMIC COMMITTEE

February 8, 1961

Mr. William McChesney Martin, Jr.
Chairman
Board of Governors of the
Federal Reserve System
Washington, D. C.

Dear Mr. Martin:

This will confirm our invitation and the arrangements which our staff has made with you to appear as a witness before the Joint Economic Committee at hearings on the Economic Report of the President. You are scheduled to appear Tuesday afternoon, February 21, at 2:00 o'clock in the Auditorium, New Senate Office Building. The discussion will deal with monetary policy for the coming year.

We hope that it will be possible for you to confine your introductory remarks to 30 minutes or less so that substantial time will be available for discussion and questions.

It would aid the Committee and the press if we could have 75 to 100 copies of your opening statement preferably by Monday, February 20. Copies sent by mail should be addressed to John W. Lehman, Joint Economic Committee, Senate Post Office, Washington 25, D. C. If the copies are being delivered by special messenger they should go to Room G-133, New Senate Office Building.

Attached is the press announcement of the list of witnesses for the current hearings.

Sincerely yours,

Wright Patman

Wright Patman
Chairman

2/9

Mr. Martin

We haven't received the confirming letter as yet--but your appearance is listed on the attached schedule for 2 p.m. the afternoon of Tuesday, February 21.

mnm

Lehman -- 5171

FOR IMMEDIATE RELEASE
February 8, 1961

CONGRESS OF THE UNITED STATES
JOINT ECONOMIC COMMITTEE

Chairman Patman Announces Hearings
on the President's Economic Report
and the Economic Situation and Outlook

Representative Wright Patman (D., Texas), Chairman of the Joint Economic Committee, has announced plans of the Joint Committee to hold hearings, beginning February 9, on the President's Economic Report and the economic situation and outlook.

Under the Employment Act of 1946, the President's Economic Report is referred to the Joint Economic Committee, which is to review it and "...file a report with the Senate and the House of Representatives containing its findings and recommendations with respect to each of the main recommendations made by the President in the Economic Report and . . . to make other reports and recommendations to the Senate and House of Representatives as it deems advisable."

The Committee has approved a plan for hearings as set forth in the attached schedule of witnesses and subjects.

Joint Economic Committee

Wright Patman, Representative, Texas, Chairman
Paul H. Douglas, Senator, Illinois, Vice-Chairman

House of Representatives	Senate
Richard Bolling, Missouri	John Sparkman, Alabama
Hale Boggs, Louisiana	J. W. Fulbright, Arkansas
Henry S. Reuss, Wisconsin	William Proxmire, Wisconsin
Martha W. Griffiths, Michigan	Claiborne Pell, Rhode Island
Thomas B. Curtis, Missouri	Prescott Bush, Connecticut
Clarence E. Kilburn, New York	John Marshall Butler, Maryland
William B. Widnall, New Jersey	Jacob K. Javits, New York

John W. Lehman, Clerk and
Acting Executive Director

SCHEDULE OF HEARINGS ON THE
1961 ECONOMIC REPORT OF THE PRESIDENT
AND THE ECONOMIC SITUATION AND OUTLOOK

Thursday, February 9, 10:00 a.m. -- Old Supreme Court Chamber
Senate Wing, Capitol

The Economic Outlook for 1961 -- Panel Discussion

Outlook for Federal, State, and local government expenditures, and for inventories, plant and equipment --

LOUIS J. PARADISO, Assistant Director-Chief Statistician,
Office of Business Economics, U. S.
Department of Commerce
Washington, D. C.

Outlook for housing construction and consumer expenditures --

GEORGE CLINE SMITH, Vice President-Chief Economist
F. W. Dodge Corporation
New York, N. Y.

Outlook for labor force and employment --

EWAN CLAGUE, Commissioner
Bureau of Labor Statistics
U. S. Department of Labor
Washington, D. C.

Outlook for demand and supply of funds and interest rates--

ROY REIERSON, Vice President and Economist
Bankers Trust Company
New York, N. Y.

Outlook for agriculture --

GEORGE BRANDOW, College of Agriculture
Pennsylvania State University
University Park, Pennsylvania

Thursday, February 9, 2:00 p.m. -- Old Supreme Court Chamber
Senate Wing, Capitol

Labor and Management Comments on the Economic Report and the Economic Situation and Outlook

Labor Comments	
2:00 p.m.	AFL-CIO WALTER P. REUTHER Chairman Economic Policy Committee
Management Comments	
3:00 p.m.	Chamber of Commerce of the U.S.A. EMERSON SCHMIDT Director of Economic Research
3:30 p.m.	National Association of Manufacturers GEORGE G. HAGEDORN Director, Research Department

Friday, February 10 -- Auditorium, Room G-308, New Senate Office Bldg.

Additional Comments by Other Group Representatives

10:00 a.m. (Panel Discussion)	American Farm Bureau Federation W. E. HAMILTON Director of Research
	National Farmers Union ANGUS McDONALD Assistant Director of Legislative Services Division
	National Grange HERSCHEL D. NEWSOM Master
11:30 a.m.	Committee for Economic Development HERBERT STEIN Director of Research
12:00 Noon	Federal Statistics Users' Conference ROYE L. LOWRY, Executive Secretary or HOWARD L. STIER, Trustee

Monday, February 20, 10:00 a.m. -- Auditorium, New Senate Office Bldg.

Council of Economic Advisers

WALTER W. HELLER, Chairman
JAMES TOBIN
KERMIT GORDON

Monday, February 20, 2:00 p.m. -- Auditorium, New Senate Office Bldg.

DAVID E. BELL
Director
Bureau of the Budget

Tuesday, February 21, 10:30 a.m. -- Auditorium, New Senate Office Bldg.

C. DOUGLAS DILLON
Secretary of the Treasury

Tuesday, February 21, 2:00 p.m. -- Auditorium, New Senate Office Bldg.

WILLIAM McCHESNEY MARTIN
Chairman
Board of Governors, Federal Reserve System

Wednesday, February 22, 10:00 a.m. -- Old Supreme Court Chamber
Senate Wing, Capitol

CHARLES J. HITCH
Assistant Secretary of Defense (Comptroller)
Department of Defense

January 27

Note:

Mr. Shay advised that hearings were now being set for testimony on the President's Economic Report--by the Joint Economic Committee.

2 pm

2:30 the afternoon of Tuesday, February 21 is tentatively set for Mr. Martin's appearance (although this is FAC day)

Hearings will start on the 9th--

On the 20th will appear members of the Council of Economic Advisers in the morning; budget bureau officials in the afternoon

On the 21st Dillon will testify in the morning; with Mr. Martin scheduled for the afternoon

A Mr. Hitch of the Defense Department is scheduled for the morning of ~~Wxxxxxx~~ Wednesday, the 22nd (G. W.'s birthday and a holiday)

THE SECRETARY OF THE TREASURY
WASHINGTON

March 6, 1961

Dear Bill,

I thought you might like to see the attached advance copy of my statement tomorrow morning before the Joint Economic Committee.

Sincerely yours,

Douglas

Douglas Dillon

The Honorable
William McChesney Martin
Chairman, Board of Governors
of the Federal Reserve System

Attachment

HOLD FOR RELEASE ON DELIVERY

TREASURY DEPARTMENT
Washington

STATEMENT OF THE HONORABLE DOUGLAS DILLON
SECRETARY OF THE TREASURY, BEFORE THE
JOINT ECONOMIC COMMITTEE,
TUESDAY, MARCH 7, 1961, 10:00 A.M.

Mr. Chairman, I am pleased to meet with this distinguished Committee. It is important that we discuss the broad outlines of our economic situation and the economic programs the Government should follow in pursuit of our central national objective.

This objective, simply stated, is to preserve and develop the security, freedom and prosperity of the United States within a strong free world. Our economic policies, both domestic and foreign, can be used effectively to serve our central objective if they are directed particularly at three specific economic objectives which have been a subject of particular concern to this Committee during the past year.

The first national economic objective is that stated in the Employment Act of 1946, namely, the maintenance of a high level of employment or, in the words of the Act, "maximum employment."

During the intervening years, marked at various times by unanticipated price rises, attention shifted to the problem of inflation and reasonable price stability emerged as a second national economic objective.

More recently, a third national objective has received increasing emphasis -- to develop economic policies directed at stimulating maximum sustainable rates of growth within our own country and within the economies of our friends and allies.

In pursuing these national economic objectives it is important to keep in mind other national objectives such as national security, a desirable degree of economic freedom, a maintenance of a market mechanism unimpaired by the absence of workable competition, the provision of adequate government services in areas where private action will not suffice, and some equitable distribution of income and opportunity.

It is only realistic to recognize that some courses of policy and action can serve to promote the achievement of certain of our goals at the sacrifice of others. It seems important that we search for and employ those economic policies which are best designed to achieve a maximum of all of these desirable objectives, without unduly sacrificing one at the expense of another.

D-35

In moving now, in the year 1961, towards these long-range national economic objectives, we must recognize the urgency of the two major problems immediately confronting us:

First, the problem of bringing about a prompt recovery from the present recession and, even more important, a continuing, vigorous expansion in our domestic economy.

Second, curing the long standing imbalance in our international payments, and working in concert with other industralized nations toward a more permanent equilibrium.

The simultaneous occurrence of recession and acute balance of payments difficulties posed new and complex problems for the United States last year. The sensitive inter-relationship between our domestic economy and our balance of payments situation can be expected to remain with us in the future. For today we face an international economic situation quite different from anything we have seen for over thirty years. This new situation arose two years ago with the return of convertibility in Europe. For the first time since the thirties all the major currencies of the free world became freely interchangeable for current transactions.

This new situation severely aggravated our balance of payments problem last year and, in turn, it determined the nature of some of our responses to recession here at home.

To begin with, I should like to review briefly the significant developments in our balance of payments in recent years.

Between 1951 and 1957 foreign countries utilized the proceeds of their surpluses, averaging roughly one billion dollars a year, to build up needed reserves of dollars. The situation has been quite different since 1957. In 1958 and 1959, our exports fell off sharply and our imports rose. Our deficit rose to $3-1/2 billion and more a year and we had to pay out some $3 billion in gold to cover a large part of this deficit. In 1960 another over-all deficit of $3.8 billion occurred and we paid out another $1.7 billion of gold.

The situation in 1960 was dominated by a new element. Our exports had a very good year. But a very large outflow of short term capital took place, mainly from June to the end of the year. Our basic deficit -- that is, minus the short term capital outflow -- markedly improved, and was estimated at about $1-1/2 billion, as against something over $4 billion in 1959. The outflow of short term capital, amounting to more than two billion dollars, was the major factor in the large drain of gold and dollars during the final six months of last year.

Now what caused this new phenomenon-- the large scale exodus of short term capital?

With convertibility, international money markets have again become closely inter-connected and liquid funds now flow freely in large volume between these markets in response to differentials in interest rates, as well as to speculative considerations. When recession here coincided with boom abroad from mid-1960 onward, monetary policies and interest rates in the United States and Europe diverged widely. At one time last fall a short term investor could obtain as much as two percent more on his money in London than in New York. Hence, a broad stream of short term capital moved from New York to London and other European money centers in search of these higher short term rates. The size of this flow shook confidence in our ability to maintain the value of the dollar. Speculation began against the dollar and added to the outflow. This speculative fever continued unabated until late January.

The first task of this Administration was to restore confidence and put an end to these speculative movements. The President promptly pledged that the official dollar price of gold would be maintained at $35 per ounce. He also outlined a broad and comprehensive approach to achieving an over-all equilibrium in our international payments, placing heavy emphasis on expanding our exports. He rejected protectionism as ineffective and undesirable and stressed that help for the less developed countries from all the economically advanced countries must be enlarged.

I am pleased to report that reaction abroad to the President's vigorous and determined approach has been very favorable. The dollar once again is strong. There has been a decided slackening in the outflow of gold and dollars and there are signs that some of the speculative funds that left our shores last fall are beginning to return.

This is not, of course, a sign that the problem is over, but only that the world believes that we mean what we say. It is imperative, therefore, that we press on with more fundamental measures for correcting our basic balance of payments deficit, utilizing the breathing spell provided by this free world vote of confidence. It is clear that achievement of reasonable equilibrium in our balance of payments will not be a simple task. It will involve vigorous and many-sided action by our government, the cooperation of other free countries, and active and enlightened support by our own people. I am increasingly hopeful that if we utilize these elements, properly welded together, we can reach our goal within the next two years.

One inescapable conclusion which emerged from the short term capital movements of 1960 is the need for more effective international cooperation in economic and monetary policy in order to minimize the disruptive effects, and the magnitude of such movements. To be sure there will always be differences among countries in the timing of booms and recessions, and there will always be some need for a short term capital flow. But if fuller exchanges of views and experience among the financial officials of leading countries can in any way reduce the impact of these swings, we must seek such exchanges. We hope to pursue this cooperation through the proposed new Organization for Economic Cooperation and Development (OECD), through the International Monetary Fund, and in other appropriate ways. At longer range, we are instituting a thorough exploration of measures to improve the functioning of the International Monetary Fund and to strengthen its capabilities, in order to assure adequate and flexible liquidity for the growth that lies ahead.

I have said that we must utilize the time given us by the restoration of confidence to attack the problem of our basic deficit, which last year amounted to about $1.5 billion. In dealing with this basic deficit, we are actively pursuing the specific lines of policy laid down by the President. For example, we expect to tie our military procurement and economic aid expenditures even more closely to United States sources of supply. We are preparing to improve our facilities for providing credit to our exporters. We are moving vigorously to promote an increased stream of tourists to the United States. We are recommending a reduction in tourist allowances. We are developing procedures to encourage foreign monetary authorities to hold dollars. And we are reexamining the tax status of American investment abroad to determine whether it is paying its fair share of our national tax and whether or not any deficiency of our tax system in this regard has contributed substantially to an imbalance of payments. We will continue to explore ways and means of assuring that the substantial payment imbalances of recent years are not continued so as to impair our national economic position.

But improvement in our basic deficit also means that the chronic surplus in the balance of payments of certain other advanced countries needs to be simultaneously reduced. This calls for improved international cooperation across the broad spectrum of economic policies. International cooperation is also increasingly needed in approaching what are now mutual responsibilities for a rising flow of capital to the less developed countries. We hope to facilitate both of these types of cooperation through the OECD.

It is also essential for our people to realize that we are inevitably subject to international competition. Just as this country has always found open competition to be a major force in stimulating growth, expansion, and technological change here at home, the same is proving to be true internationally. This development serves to emphasize our need to remain strong and competitive -- and not restrictive or isolated. Obviously, this has a great many implications for American industry in terms of the price-wage-cost structure. It becomes important to emphasize to both management and labor that profits and wages need not always be increased to provide more benefits to investors and workers. Both of these economic groups are made up of individual consumers. Hence, the provision of more goods and services for the same dollar by some lowering of prices with increasing productivity may better distribute the benefits of that increased productivity between workers, investors, and consumers, without sacrificing our international competitive position. The President has just provided a channel for funnelling many of these considerations and bringing them to bear on key problems through the President's Advisory Committee on Labor-Management Policy.

Now to return to the problems of our economy here at home. We must try to produce an environment that will not only bring us out of our present recession, but will also permit our economy to grow at a faster rate than has been the case in recent years.

The role of the Federal Government as an energizing force in the growth of our economy and as a stabilizing influence upon its ups and downs is daily becoming more important. But there are limits upon what the Government can, or should, do. It is as important to avoid over-commitment as under-commitment, as essential to avoid waste as to avoid constrictive economy. We must make certain that the powerful and productive influence of the Federal Government is used most effectively.

Our nation's resources -- the capacity of our people and the quality of our physical plant and materials -- are impressive. But they are not presently being fully utilized and the level of unemployment is unacceptably high. In initiating new programs of expansion, therefore, we can call upon unused resources, upon credit ease and fiscal expansion -- and even upon a reasonable budget deficit for a limited period of time -- without running the risk of inflation.

There are, of course, inescapable physical limits on the speed with which our untapped reserves can be put to use. Nevertheless, the current recession makes a modest and temporary deficit not only inevitable, but actually desirable as a stimulant to recovery and the resumption of economic growth. The fact is that a budget deficit may prove helpful in a period of widespread unemployment such as the present one. During periods of prosperity, of course, we should return to balanced budgets and surpluses.

It is now clear that revenues in fiscal 1962 cannot help but be less than those projected in President Eisenhower's final Budget Message of January 16. In that message, corporate profits for calendar 1961 (on which, of course, fiscal 1962 revenue figures are based) were estimated at forty-six billion dollars. The facts now available indicate that this estimate is too high, possibly by as much as three billion dollars. In addition, personal income may fall somewhat short of the four hundred fifteen billion dollar estimate in that Message.

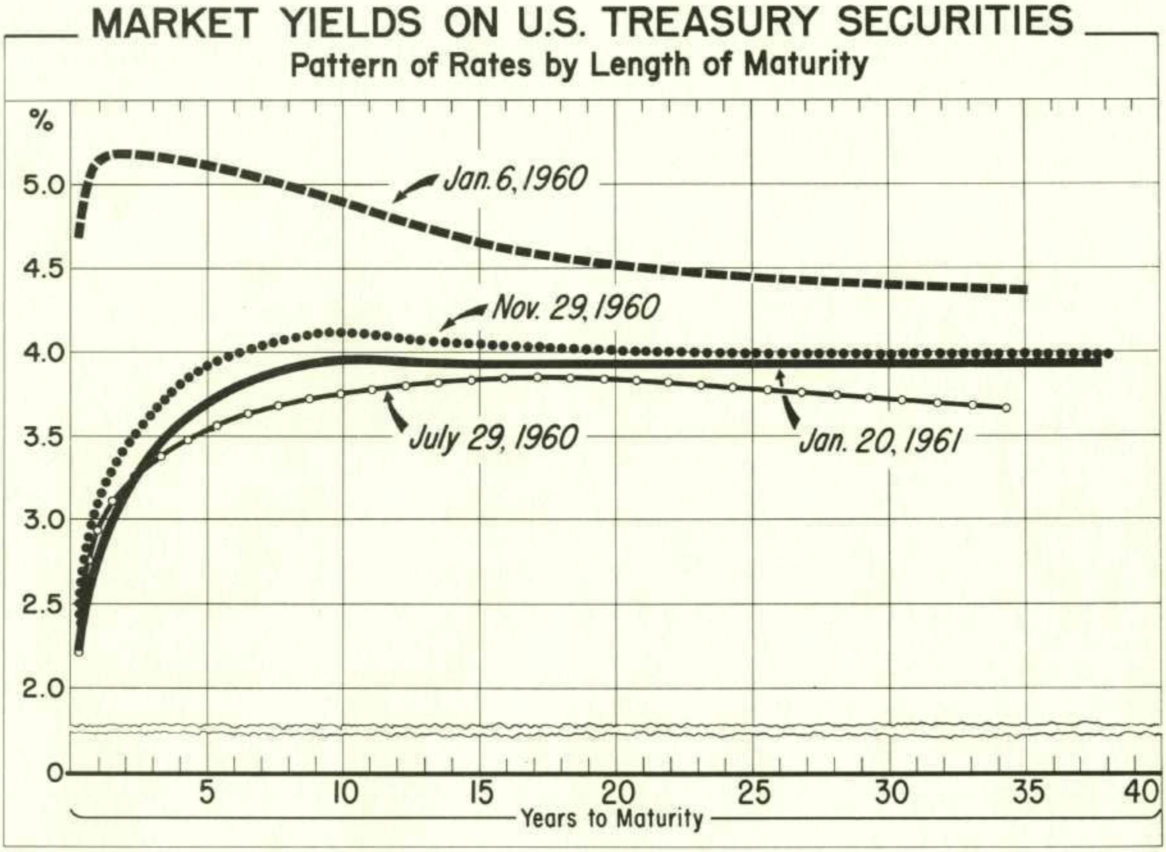
I cannot pinpoint revenues and expenditures more exactly since final decisions have not yet been taken by the President. However, the Director of the Budget will be able to provide you with these estimates when he appears before you later this month.

In past recessions the Federal Reserve has been able to promote the needed lower long term rates of interest by allowing the short term rate to fall almost to zero. In 1958, for instance, ninety day bills sold at six-tenths of one percent. This tended to lower long term rates and in turn promoted economic recovery. It is important here to recognize that extremely low short term rates are not of themselves necessary for recovery. They reflect increased credit availability and help stimulate the investment flow into the long term sector at lower rates. Today, a reduction in long term interest rates, including mortgage rates, is just as necessary as in previous recessions, but we must find new tools to achieve it. No longer can extremely low short term rates be permitted to result from credit easing steps taken to achieve our recovery objective. Instead, moves have been made to stabilize the short term rate around present levels, an adequately low rate for business purposes. There is always the danger that a lower rate may precipitate a renewed flow of short term capital abroad which could once again affect confidence in the soundness of our dollar. This we cannot allow to occur.

Therefore, other means must be found to promote lower long term rates -- means that they do not immediately involve downward pressures on short rates. It was this dilemma that led the Federal Reserve Board to the conclusion that the "bills only" policy which had worked effectively in earlier recessions was no longer appropriate to the task at hand. In addition, the Treasury can and should support efforts to lower the long term rate by judicious debt management policies, not forgetting, however, the need for some lengthening of the debt so as to maintain a reasonable refunding pattern.

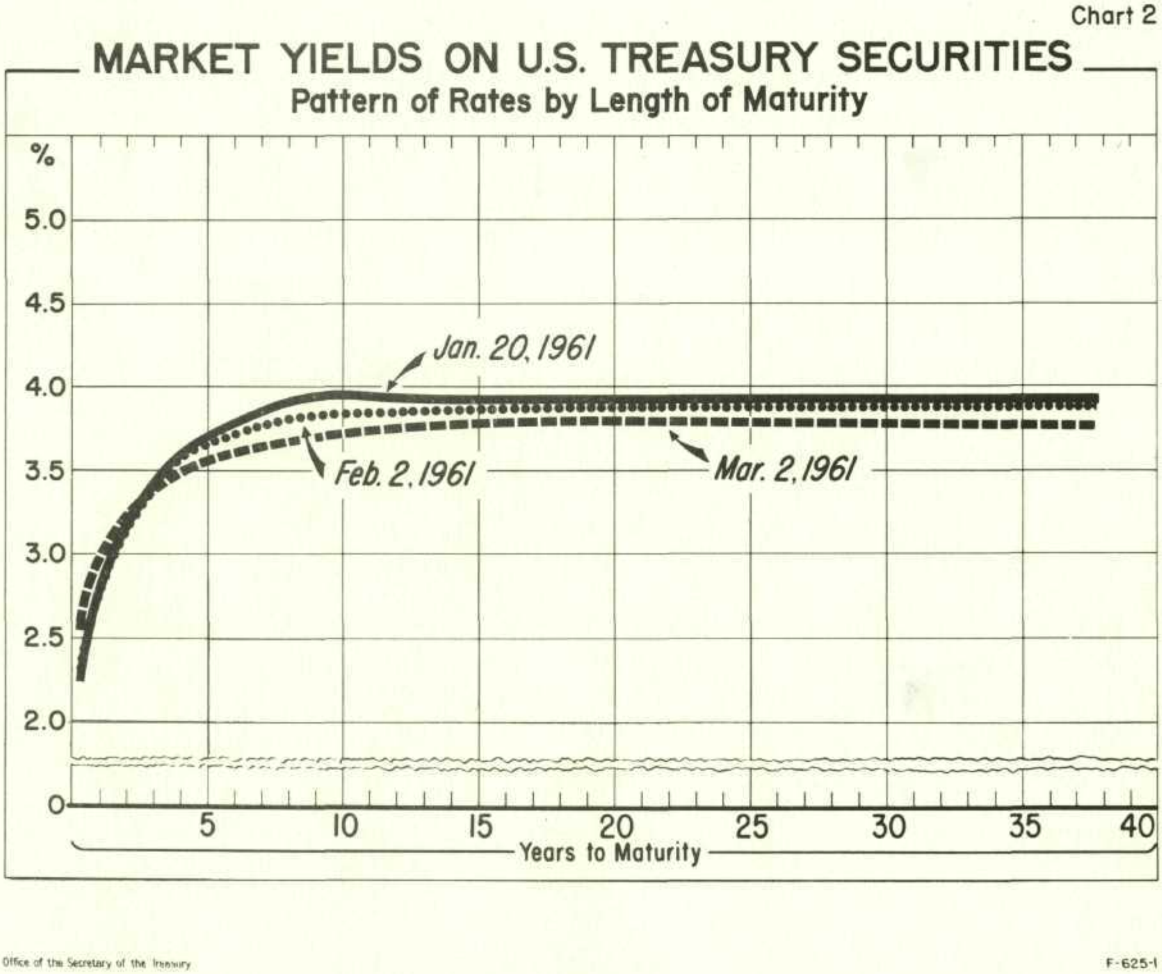
Recent developments in this field can be seen from the two charts before you which show the market yields on U. S. Treasury securities for selected dates.

Chart I



Office of the Secretary of the Treasury F-625-2

The first chart shows that the high point last year was reached in January, and the low point the following July. It also clearly shows that long-term rates actually moved up as the recession deepened toward the end of last year -- indicative of a lag in the availability of credit to borrowers.



The second chart shows that a decline in rates has occurred since Inaugural Day and that a further decline followed the President's economic Message, in which he specifically called for maintaining short rates at current levels and a greater availability of long-term credit at declining rates. This decline in long term rates, coupled with the maintenance of short term rates was helped when the Federal Reserve last month began buying government notes and bonds of varying maturities, some beyond five years, for virtually the first time in a decade, and the Treasury concentrated its sales of securities in the short-term sector. The effect of these policies is, of course, to decrease the supply of long-term securities and increase the supply of short term securities.

Our attempts to try to bring about a greater availability of credit at lower interest rates in pursuing recovery and growth are certainly justified by recent developments. There has been a notable lag in certain key areas such as housing and municipal and corporate investment. Yet these are the very areas which we wish to stimulate.

Let me briefly examine these three specific areas:

First, housing: Although in housing the availability of credit at lower mortgage rates is only one aspect of the problem, it is nevertheless an important one. We are hopeful that efforts of the Administration to lower mortgage rates -- by reducing the Federal Housing Administration rate, placing more emphasis in the Federal National Mortgage Association program on buying rather than selling mortgages, and urging key mortgage lenders to lower their rates -- will help to speed up a decrease in long-term mortgage rates reflecting the increase in available mortgage funds that is already beginning to manifest itself.

Second, security offerings of municipalities, state, and local governments: Ordinarily, as interest rates decline and funds become increasingly available in a recession period, such offerings increase. However, in the current recession, this pattern has not been discernible. As late as last month, offerings continued to lag somewhat below a year ago. But as the credit ease continues, we can expect some growth in constructive municipal borrowing. Estimates for March project a considerable increase over the corresponding month last year.

Third, the corporate financing field, where the stock market seems to be openly inviting additional equity financing -- an invitation we hope will be increasingly accepted by corporations. For the more corporations turn to the securities markets and repay their bank loans, the more the banks will be able to supply credit to other borrowers, and so stimulate recovery.

There is another vital force in this whole area of interest rates and the availability of funds generally, and that is in the field of tax policy.

I shall defer discussion of this subject in view of the recommendations which the President proposes to submit shortly on tax measures that will encourage the expansion and modernization of the Nation's productive plant so as to accelerate economic growth and improve the international competitive position of American industry. It will perhaps suffice to state the basic goal of our tax policy. It is simply this: to develop and maintain a strong tax system which will meet the revenue requirements of the Government, contribute to economic stability, and further the objectives of a dynamic and growing economy.

The tax system should be flexible and respond to changing economic conditions. In times of falling income, the receipts under such a tax system should decline, so that resulting Federal Budget deficits will help to sustain the level of demand and employment. In times of rising income and employment, the system should furnish increasing revenue and a surplus should result. An important advantage of the surplus will be that through debt retirement, it can be made available to private investors for capital formation and economic growth. We are looking forward to a strong economy in which such years of surplus will match or exceed those of deficit.

The problems of bringing about a prompt recovery and, more importantly, vigorous expansion, call for the stimulating potential of a larger Government budget within a financially orderly framework. We aim to make Government's contribution to economic activity in a way that will provide solid support -- rather than more temporary stimulus -- to the flourishing and continuing growth we can and must achieve. We hope that by carring out these many-sided programs with resolve and determination, we can make maximum use of our resources, both human and material, to create a brighter future for all Americans.

oOo