

NOMINATION OF GEORGE W. MITCHELL

HEARING
BEFORE THE
COMMITTEE ON BANKING AND CURRENCY
UNITED STATES SENATE
EIGHTY-SEVENTH CONGRESS
FIRST SESSION
ON
THE NOMINATION OF GEORGE W. MITCHELL TO BE A
MEMBER OF THE BOARD OF GOVERNORS OF THE FED-
ERAL RESERVE SYSTEM FOR THE REMAINDER OF THE
TERM OF 14 YEARS FROM FEBRUARY 1, 1948

AUGUST 15, 1961

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NOMINATION OF GEORGE W. MITCHELL

TUESDAY, AUGUST 15, 1961

U.S. SENATE,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D.C.

The committee met, pursuant to the call of the chairman, in room 5302, New Senate Office Building, at 10:05 a.m., Senator A. Willis Robertson (chairman) presiding.

Present: Senators Robertson, Sparkman, Douglas, Clark, Proxmire, Williams, Long, Capelhart, Bennett, Javits, and Tower.

Senator SPARKMAN (presiding). Let the committee come to order, please.

The purpose of the meeting this morning is to consider the nomination of Mr. George Wilder Mitchell, of Illinois, to be a member of the Board of Governors of the Federal Reserve System for the remainder of the term of 14 years to February 1, 1962, in the place of Mr. Szymczak, who has resigned.

Mr. Mitchell, we are glad to have you with us. We have a Senator from your State, Senator Douglas, as a member of this committee.

Do you have a prepared statement to give?

Mr. MITCHELL. No, I do not.

Senator SPARKMAN. Would you like to tell us something about yourself?

May I say that we have your biographical sketch, and it will be printed as part of the record.

(The biographical sketch of Mr. Mitchell follows:)

Mitchell, George Wilder, economist; born Richland Center, Wis., February 23, 1904; son of George Ray and Minnie (German) Mitchell. Married Grace Marion Muir, August 30, 1927; children—Marilyn Anne (Hagberg), Bruce William, Judith Nancy (Rediehs), Margery Grace.

A.B., University of Wisconsin, 1925; student (part time), University of Iowa, 1927-30, University of Chicago, 1930-33.

Research assistant, University of Wisconsin, 1925-26; statistical and research assistant, United Typothetae of America, 1926-27; instructor and research assistant, University of Iowa, 1927-30; research assistant, University of Chicago, 1930-33; director of research, Illinois Tax Commission, 1933-39, 1941-43 (member of commission, 1939-40); assistant to director, Department of Revenue, State of Illinois, 1943; director, Department of Finance, State of Illinois, 1949-51; tax economist, Federal Reserve Bank of Chicago, 1944-48, vice president, 1951-.

Tax consultant for Civil Aeronautics Board and director of study of multiple taxation of air commerce, 1944-45; member of advisory group appointed by Joint Committee on Internal Revenue Taxation to Investigate the Bureau of Internal Revenue, 80th Congress; chairman of Federal Reserve Committee which prepared "Automobile Installment Credit Terms and Practices," supplement III, Federal Reserve System, "Consumer Installment Credit," part I, volume 2, 1957; chairman of Federal Reserve Committee on Surveys of Credit and Capital Sources, U.S. Congress, "Financing Small Business," part 2, 1958; member of Illinois Governor's Revenue Commission, 1961; member of National Committee on Government Finance, Brookings Institution, 1961-.

Member of American Economic Association, American Finance Association, National Tax Association (president, 1948), Institut International de Finances Publiques, International Association of Assessing Officers, Tax Institute, Regional Science Association, Delta Sigma Rho, Phi Kappa Phi. Member of Congregational Church.

Additional publications: editor of 8-volume "Survey of Local Finance in Illinois," 1939-40; coauthor of "Business Activity in Iowa," 1930; "Assessment of Real Estate in Iowa and Other Midwestern States," 1931.

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STATEMENT OF GEORGE WILDER MITCHELL, CHICAGO, ILL.

Mr. MITCHELL. Let me say that when I graduated from the University of Wisconsin in 1925 I was uncertain whether I would go into teaching or into administration or research; and during the course of the next few years, having tried all of these, I decided upon research and administration.

I spent approximately 11 years in tax administration in the State of Illinois, working as director of research for the Illinois Tax Commission, and was finally named a member of the commission. I went to the Federal Reserve Bank of Chicago in 1944 and have been vice president in charge of research at that bank since 1951.

In the course of the years at the Federal Reserve Bank of Chicago, I had a leave of absence to act as director of finance for the State of Illinois. The director of finance functions are principally the preparation of the State budget and the determination of fiscal policies for the State government.

I also had a leave of absence to work for the Civil Aeronautics Administration on a study of multiple taxation of air carriers, and another leave to serve as a member of a committee appointed by the Joint Committee on Internal Revenue Taxation to investigate the administration of the Bureau of Internal Revenue.

This recital of highlights in my career indicates, I think, that I have been in the public service almost throughout my entire career.

Senator SPARKMAN. Senator Proxmire?

Senator PROXMIRE. Yes.

Senator SPARKMAN. This gentleman is not a constituent of yours now, but he used to be when you were a resident of his State.

Senator PROXMIRE. You can almost say he was a constituent by proxy.

Senator SPARKMAN. You were in Illinois when he was in Wisconsin.

Senator PROXMIRE. Yes. Mr. Mitchell was born in Richland County, Wis. We are very proud of Mr. Mitchell's fine record.

This is a very splendid appointment. Here is a man who has a most pertinent kind of background in the Federal Reserve System, and also has a quite broad experience outside the Federal Reserve System. So it is not a matter of appointing a man who has spent his whole life within one agency.

However, I would like to ask Mr. Mitchell some questions, because I think that Senator Morse raised a point on the floor of the Senate about 4 or 5 days ago as to the dangers of appointing people from within a particular agency to that agency. Such persons may get a very narrow viewpoint and tend to look at the agency from the standpoint of the regulative units within the industry, in this case the banks,

rather than having a broader perspective, which is useful in making policy decisions.

With this in mind, I would like to ask to what extent, Mr. Mitchell, would you say that the interest rate is determined in a free market by the forces of demand and supply?

Mr. MITCHELL. The interest rate, of necessity, is determined by the demand for funds, both short and long term, generated by the Government, individuals, corporations, and others who use money, and by the supply, which is generated by the savings of individuals and corporations and the reinvestment by individuals and financial institutions. To these sources of supply we should add the capacity of the banks to expand their use of credit through the operations of the Federal Reserve System.

Senator PROXMIRE. What I have in mind is: Isn't the level of interest rates something that can be determined by policies deliberately adopted by the Federal Reserve Board? Since 1914, isn't the history of the Federal Reserve Board one of stepping in whenever they felt it desirable to do so and increasing or decreasing interest rates to moderate the economy one way or the other, either to stem a possible inflation as they did in 1929, or to stimulate activities as they did in the depression period during the early thirties? Hasn't there been a long history of this?

Mr. MITCHELL. A long history of moderating or affecting changes in interest rates. When you say "determine," this gives rise to the possibility that one might say the Federal Reserve could fix the interest rate anywhere at any point. I think this is not the case, except with disastrous consequences.

Senator PROXMIRE. They may not be able to fix a precise rate at a specified time. But isn't it true they can pretty much fix it because they control the supply of money? The Constitution requires that the Congress have control over the supply of money, and Congress has delegated that control to the Federal Reserve Board. The Federal Reserve Board can increase or decrease the supply of money as they wish.

Mr. MITCHELL. From the supply side, as I indicated, this is only one source of supply of credit to meet the various demands for credit. The other sources are the savings of individuals and corporations and the stream of reinvestment funds which is coming on the market and seeking reinvestment. To this you add the amount of credit that the banks can extend, which, in turn, depends on the monetary policy being followed at that time by the Federal Reserve System.

Senator PROXMIRE. This is one area that traditionally is not a matter of much controversy. There is some. Traditionally, the Government can have a direct impact on the economy by determining the supply of money. The Government can, and the Government does. It is recognized as good public policy. And we don't have to argue about it as we do about fiscal policy—spending, and so forth.

Mr. MITCHELL. Yes, that is right. But again, as I say, this is only one factor in determining the level of interest rates.

Senator PROXMIRE. With that in mind, on page 38 of this very interesting report of the Commission on Money and Credit, it is argued that at some level of unemployment, an increase in demand is not inflationary. I think the figure they use is 8 percent. They say if

unemployment gets to a level of 8 percent, we can increase demand sharply and substantially. There is little or no inflationary effect.

Mr. MITCHELL. Yes.

Senator PROXMIRE. The inflationary effect is minimal. Would you agree with this?

Mr. MITCHELL. With the level of unemployment at 8 percent, I would say an increase in demand would not be inflationary; that is right.

Senator PROXMIRE. We have a level of unemployment now which is 7.3 percent unadjusted and 6.9 percent seasonally adjusted. It is very high. It is close to the 8-percent level.

Mr. MITCHELL. That is right.

Senator PROXMIRE. Under these circumstances, would you say that an increase in the supply of money which, of course, I take it, does have the effect of increasing demand, would be inflationary?

Mr. MITCHELL. No.

Senator PROXMIRE. It would not be? Would not that have the tendency to make funds more available and therefore tend to promote employment?

Mr. MITCHELL. Yes.

Senator PROXMIRE. All right. I don't want to take too long because I think other Senators should have an opportunity to question you, and I know they are all busy. I should like to suspend my questioning now and come back a little later. I don't want to detain the nominee at any length, but I think other Senators might be desirous of going ahead.

Senator SPARKMAN. Very well. Senator Bennett?

Senator BENNETT. Only one comment: You have made it clear at least to me that the power of the Federal Reserve and its actions represent only one factor in all of these powers and actions that finally control the current rate of interest. Am I correct in assuming that?

Mr. MITCHELL. Yes, sir.

Senator BENNETT. My friend from Wisconsin has rather pushed you to the point where I think he would like the record to show that the Federal Reserve can determine the supply of money. I think you answered "yes" to that question.

Mr. MITCHELL. The supply of money; yes, that is true. The Federal Reserve can determine the supply of money, but this is not the same thing as saying that it can determine the rate of interest.

Senator BENNETT. Actually, what the Federal Reserve does is use its power to increase a part of the supply of money. It does not control all of the supply of money.

Mr. MITCHELL. Yes, sir; you are right. What the Federal Reserve does is provide the reserves for the banking system. The business and individual community decides how these reserves are going to be used—and the banks, too. It may be that they will be used by an increase in private demand deposits, which are a part of the money supply. Some of the reserves may go into currency; in which case they become a part of the money supply.

Some may go into Government deposits temporarily. The Government's balance may rise. This absorbs reserves, but does not affect the money supply. Ordinarily, it is a short-run phenomenon. It may be that the Federal Reserve is attempting to expand the money sup-

ply by providing additional reserves to the banking system. The immediate reaction may be that Government deposits rise and this is all that happens. Some may say the Federal Reserve isn't doing anything. The Federal Reserve has done its bit, but it takes the time for the Government to spend this balance and draw it down before the money gets into the private hands and then becomes a part of the money supply.

The other thing that can happen to the reserves is they can go into time deposits; and if they do go into time deposits, they don't get into the money supply, as conventionally defined. Milton Friedman, for example, defines the money supply to include time deposits. He is almost alone with respect to this.

So actually reserves provided by the Federal Reserve get into the money supply as a result of what banks and businesses and individuals do. Of course, if the banks permit the reserves to lie idle, individuals do not even get a chance to operate in this respect.

Senator BENNETT. It seems to me that private individuals and corporations, by their savings and reinvestment, provide most of the money supply and the Federal Reserve can influence this volume as a kind of residual or marginal effect.

If the Federal Reserve System supplied all the money, we would have complete fiat money and our system would have lost its basic pattern.

Mr. MITCHELL. Senator, I think our difficulty is just a semantic one. When you say money supply, you are saying what I ordinarily mean by the term "supply of credit." The phrase that I use is "supply of credit." The supply of credit depends upon the amount becoming available for reinvestment on people's predilections to go long after being short, on the savings in the community and the amount of credit created by the Federal Reserve System.

Senator BENNETT. Changing the word, then, the amount of credit that the Federal Reserve supplies is not the basic amount of credit in our economy.

Mr. MITCHELL. That is right; yes, sir.

It adds to it or any detract from it.

Senator BENNETT. To that extent it affects the interest rate.

Mr. MITCHELL. That is true.

Senator BENNETT. But it is not the sole factor?

Mr. MITCHELL. Yes, sir; it is not the only factor.

Senator BENNETT. I have no other questions, Mr. Chairman.

Senator SPARKMAN. I should have added earlier that we have the approval of the two Senators from Illinois to this nomination, both Senator Douglas and Senator Dirksen. Senator Douglas, have you any questions to ask or comments to make?

Senator DOUGLAS. Mr. Mitchell is a man of very high qualifications for this position. We all have before us the sheet giving his past achievements, which show that he is splendidly prepared for a position on the Federal Reserve Board for the remainder of Mr. Szymczak's term.

He has been vice president of the Federal Reserve Bank in Chicago, and a director of their research division. I think probably he is one of the best qualified men that we have had before us for appointment to the Federal Reserve Board. He is a man of high character and

great integrity. And it is a source of personal satisfaction to me to see that he has been appointed.

Purely for the record, I would like to make this comment to which Mr. Mitchell may give such weight as he thinks it deserves. I have felt that the Federal Reserve Board paid very close attention to what they call the financial condition of the country and followed the credit, banking, and monetary situation very closely. I have not felt that they followed the employment conditions of the country as closely, and that they perhaps did not recognize as fully as they should their responsibility in seeking to maintain a higher level of production and employment consistent with a reasonably steady price level.

I am not going to offer any advice to Mr. Mitchell in view of his experience. But I do hope he will address the attention of the Board at least to a set of facts: First, the actual volume of unemployment in the country; and second, the degree of unused capacity in the country.

The index of unemployment in July stood at 6.9 percent, seasonally adjusted. This is based on taking as a denominator the total working force of the country and not merely those that seek wage and salaried positions. If we eliminate the 11 million self-employed, the percentage of unemployment is approximately 8 percent. Then if we take into account the involuntary part-time workers—those who work less than 37½ hours a week, although they would like to work a full week—we get an additional 2 percent unemployment. So we have involuntary lost time of approximately 10 percent at the present time, which is an extremely high ratio.

Similarly, we have a large amount of idle capacity. A fair estimate would be that 20 percent of our productive capacity is not used. With 10 percent unemployment and 20 percent idle capacity, it would certainly seem that a monetary credit policy which would aid idle men to be put to work, or idle plants to produce goods which otherwise would not be produced, would be in the national interest.

I have been struck by the fact in the past that when we tried to point this out, perhaps imperfectly, to the Federal Reserve Board, this has seemed to fall on deaf ears. I felt frustrated about it. Such a monetary credit policy has been represented as inflationary. Yet we have gone for a considerable period of time without inflationary effects, because when we get an increase in the total supply of money, we may also get an increase in the physical quantity of production. The equation of the quantity theory of money has two sides to it. And a mere increase in the amount of money does not send up the price level, if it is met with a compensatory increase in the quantity of goods.

So I am not going to ask you questions at this point. But I will merely say that these are matters which, in my judgment, have not been sufficiently considered by the Federal Reserve Board, which have not been given adequate weight by the Federal Reserve Board, and which deserve to be considered by the Federal Reserve Board.

Senator SPARKMAN. Senator Javits?

Senator JAVITS. Mr. Mitchell, what is your concept of the independence of the Federal Reserve Board from the Treasury?

Mr. MITCHELL. From the Treasury?

Senator JAVITS. Yes.

Mr. MITCHELL. I think the Federal Reserve System operates to accommodate the entire economy—agriculture, business, commerce, and government. The Federal Reserve cannot ignore the operations of the Treasury, nor can the Treasury ignore the responsibilities of the Federal Reserve System.

I think it is a case of independence to a degree, but neither should be bound by the other's decisions if these decisions involve inconsistent behavior on the part of each of them.

Senator JAVITS. So you would not feel yourself bound out of loyalty or other considerations to follow the desires of the Treasury if you believed that the total economic system called for some other decision?

Mr. MITCHELL. That is correct; yes, sir.

Senator JAVITS. And I assume you would contend for that point of view in the Board.

Mr. MITCHELL. Yes, sir.

Senator JAVITS. What do you think of the report of the Commission on Money and Credit, headed by Mr. Frazar B. Wilde? Have you had an opportunity to study it?

Mr. MITCHELL. I am generally familiar with this report, and I think, in general, the underlying philosophy of the report is appropriate and proper, and I would generally subscribe to it. As far as specific recommendations are concerned, they are extremely numerous, and some of them are helpful and others, I think, are not helpful, and some I am just indifferent about.

Senator JAVITS. Yes. I can understand that. And I wouldn't take my colleagues' time by going into that. The Joint Economic Committee is having a series of hearings on that right now.

Mr. MITCHELL. I know that.

Senator JAVITS. The last point I would like to get your philosophy on, because that is all one can do in a hearing on confirmation, is the question of the base of credit. I noticed your emphasis on savings in your answer to Senator Proxmire. I am sure you understand the basic concept enunciated by Senator Douglas. That is, the credit base, because of unused capacity and a certain amount of built-in unemployment, must have some quotient for real assets in earning power, even if not realized. I would just like to know if you have any feeling on that score.

In other words, is your view the doctrinaire view that we are limited in our credit base by the amount we save every year? Or do you feel that our yearly savings are too narrow a base for this exploding world and for our own dynamic economic situation?

Mr. MITCHELL. That relates to the relative importance of savings and reinvestment and monetary creation. Senator Douglas understands, I am sure, that at the margin a small amount may have quite an impact. It may be that savings and the stream of reinvestment—plus the amount people are willing to commit on a longer term—provides 90 percent of the credit that is needed for expansion toward full employment. The part that the monetary component, that is monetary expansion, might provide, might be relatively small, but it might have quite significant effects on the rate structure. The danger for which we must be alert is that the monetary supply is not

expanded too rapidly, and that we don't get inflation. It is really a question of judgment as to whether it is being done or not being done.

Senator JAVITS. Finally, where do you see the greatest opportunities as you enter, as I am sure you will enter, into this great responsibility? Where do you see the greatest responsibilities for the development of our economy? Let me indicate to you what I mean by that. Do you see it in increasing productivity? Do you see it in expanding foreign operations, both in aid and trade? Do you see it in raising the American standard of living? Do you see it in great sweeps of technological advance? Where do you see our great opportunity?

Mr. MITCHELL. I think, basically, it depends on technological advance. We need to do what is required to have a more productive economy, and I think this, over the long swing, is a matter of technology. Technology has given us our current standard of living, and can give us a higher standard of living.

The contribution that the Federal Reserve can make toward this is mainly in moderating cyclical swings.

Senator JAVITS. So you would put the highest premium on technology, automation, the development of the production process. You feel that the main emphasis has to be on expanding productive bases in a technological sense?

Mr. MITCHELL. I believe so.

Senator JAVITS. I think that is very enlightening and a very interesting key to your philosophy. Thank you.

Senator SPARKMAN. Senator Clark?

Senator CLARK. Mr. Mitchell, I imagine that you are as convinced, as I am sure all the committee members are, that you are going to be confirmed, without much trouble, to this very important position. My friends on either side of me who have your interests at heart tell me that you are thoroughly competent. My own very superficial look at the situation would indicate that their judgment is correct.

I shall vote for your nomination. But this is rather a curious part of the folklore of the Senate. We summon these nominees here and ask them rude questions or make dissertations on subjects about which we know very little, at least as far as I am concerned. My colleagues know far more than I. This is a kind of irresistible opportunity for a politician to sound off at least briefly on this subject.

Senator DOUGLAS. Very important, too.

Senator CLARK. I am without the self-discipline which would make it possible for me to resist this opportunity to deliver a little lecture. You are going into a highly technical job in which the exercise of professional judgment is of the greatest importance. With one or two possible exceptions, I don't think there are very many members of this committee who have the technical ability to appraise very thoroughly just what your decisions should be. But I would like to suggest to you quite briefly, Mr. Mitchell, a philosophical approach to this job.

I would start with the basic precept that one of the most dangerous things in our democracy is political and economic lag. All of our people in positions of importance, those who are appointed as much as those of us who are elected, are apt to be behind the times and unprepared to recommend and put through the steps which a constantly changing world and an incredibly fast-moving economy require. Therefore it is of the greatest importance in the world that we should

have an open and creative mind in these jobs of great technical responsibility.

The danger is that we will have negative and conventional minds which are not willing to look facts objectively in the face, but merely report and repeat the outmoded cliches of the day which is gone. Such people may have very little tolerance for new ideas, and be quite sure that the economics they learned in college—the law of profits—never changes. The conventional wisdom, as Professor Gailbreth put it, has almost the same sanctity as the Bible.

I feel myself, having been somewhat of a student of Arnold Toynbee, that the most important thing in our civilization is to have a creative minority, a dominant minority to guide our affairs. It is nip and tuck in this critical point of our history whether that will be the case or not.

You have an extraordinary opportunity to show your sound judgment. Your keen understanding of these problems and your willingness to keep an open mind will be of most importance. I don't think that some of your colleagues on the Federal Reserve Board have kept that open mind. As a result, the workings of the Federal Reserve Board have been far less satisfactory than they would have been if its present members had been a little less intransigent and a little more willing to look at changing conditions objectively.

I share the views of my colleagues that unemployment and employment are entitled to more consideration under the Employment Act of 1946 than they have had. Stability is terribly important, of course. Maximum production also is important. But employment deals with human beings. Just because a man spends his life dealing in terms of money and living with bankers and in the middle of fiscal affairs is no reason for him to lose his sense of compassion. Nor is it necessary for him to take a kind of intransigent position with respect to matters respecting human beings.

No one can be certain that it won't also lead to a sounder economy. I don't think the independence of the Federal Reserve Board is a sacred cow either. It served us well in the past; it may not serve us well in the future. Ours is the only central bank in the world not controlled by its government. Maybe this is something we should take a continuing look at.

My lecture is over, and I don't intend to solicit any reply unless you feel so inclined. I do think you are going into a position of enormous responsibility and I hope you keep an open mind.

Senator SPARKMAN. Senator Tower?

Senator TOWER. Do you feel any major organic changes should be made in the Federal Reserve System? Do you contemplate recommending any such changes? Do you believe the functions of that System should be expanded?

Mr. MITCHELL. I don't think that any major changes are needed. There are many alternative organization structures and many ways of running an organization. We may not have the best possible system right now. It seems to me, for example, that some of the CMC recommendations might result in improvement, although I would be inclined to think that if changes were to be made, perhaps more consideration should be given to those which were suggested by Professor Reagan in an article reprinted recently by the Joint Eco-

nomic Committee. He recommends the abolishing of the Federal Reserve Board and the creation of the office of Governor. That would be a drastic change, but it might be worth considering.

Just tinkering with the Federal Reserve structure is not likely to be significantly productive even though it might result in some improvement. I would like to see the base of support for the Federal Reserve somewhat broadened. Precisely how one goes about doing it, I am not entirely sure.

Other than that, I don't believe I have any comment, Senator, which is really responsive to your question.

Senator SPARKMAN. Does that complete your questioning, Senator Tower?

Senator TOWER. Yes.

Senator SPARKMAN. Senator Williams?

Senator WILLIAMS. I have been reading the New York Times profile on Mr. Mitchell. I am very much impressed. And I think I will experiment here and resist the temptation to make a dissertation.

Senator SPARKMAN. Senator Long?

Senator LONG. I am very much impressed with the philosophy of my colleagues on this committee as well as the qualifications of the nominee, so I, too, will refrain. I have no particular philosophy to express to the committee or questions I want to ask of the nominee.

Senator SPARKMAN. Senator Proxmire, do you have a few more questions?

Senator PROXMIRE. Yes. I apologize to the committee and I do not mean to detain you. This is an important occasion. This is an appointment for a few months. But it may be the prelude to a 14-year term on the Board.

The money supply is roughly 27 percent of the gross national product. This is nearly the tightest, as far as I can remember, that it has been since 1914. There may have been some other occasions when it was tighter, but not many. It is certainly the tightest in the last 30 years.

Can you cite any instances in which the ratio of money supply to gross national product was tighter than it is right now?

Mr. MITCHELL. No, sir; I don't believe I could. I would like to comment. Would you like to have me comment?

Senator PROXMIRE. Yes, I would.

Mr. MITCHELL. In the last decade, roughly, money supply has risen 26 percent. And the turnover of deposits—which is another way of measuring velocity and is not the same as income velocity—has risen 60 percent. This is the turnover in 337 centers, excluding New York, for in New York the turnover has risen 140 percent.

The net of all this is that we have had a 6 percent annual compounded increase in effective money.

Along with the secular increase in turnover, we have been getting a secular increase apparently in income velocity. I think this is the reason why it hasn't really been necessary to increase the money supply as rapidly as it would otherwise have been.

Senator PROXMIRE. Is that not always true? It is always true by definition that when we have a small money supply in relation to the gross national product, the velocity necessarily has to increase.

Mr. MITCHELL. Velocity and turnover are both responsive to rising economic activity.

But turnover in the short run doesn't have very much leeway in it. In the long run it has the leeway brought about by institutional changes. For example, the number of times people are paid has something to do with the frequency of turnover. The more often they are paid the higher the velocity.

The growth of the so-called budget or special checking account has tremendously increased the velocity of deposits. For example, the average velocity of an individual account is something between three to six times a year. Business accounts are around 25 to 30 times a year. The budget accounts are 12 to 15 times a year.

As we add to the number of budget accounts and as corporations require their treasury departments to conserve on cash, we step up velocity. This cannot be done overnight. But in the course of a decade, a great deal has been done to conserve on money needed to do the same job. In a period of boom, velocity rises slightly. It rises a little more rapidly than it does at other times, but most of the change in velocity that occurs has been occurring in the postwar years secularly, and I don't know how much further it may go. It may go quite a way. Some people say it has to stop. Obviously, it will stop someplace. But it can continue for some time.

Senator PROXMIRE. There is no question but that the velocity would automatically increase as the money supply diminishes in relation to the job it has to do with respect to gross national product.

Mr. MITCHELL. That is right.

Senator PROXMIRE. The argument that the velocity has increased doesn't seem to me to be a satisfactory answer. I pointed out that the situation is one that discourages the expansion of our economy and that tends to militate against employment on a historical basis. The policy of the Federal Reserve Board, just considering the factors of money supply and gross national product, is as tight as it has ever been in the 47 years since the Federal Reserve System was established.

Mr. MITCHELL. I think you are still talking about income velocity. Money is used for a great many things other than final purchases or product. This is what gross national product is. There are all the intermediate transactions leading up to these final transactions for which money is necessary. In addition to that, there is a tremendous volume of transfer of debt and equity for which money is needed. You are taking one small use of money, namely, gross national product, final purchase; but really one has to consider all the other uses of money, some of which are proportional to changes to gross national product and some of which are not. New York debits tend to be inversely related.

Senator PROXMIRE. Can you give me any statistics that indicate the money supply is easing? Would you characterize the present monetary situation as one of credit ease?

Mr. MITCHELL. Yes. The position of the commercial banks today is indicative of monetary ease. Business loans are not rising and investments have been rising very sharply. This always happens in a period of monetary ease.

Senator PROXMIRE. But we have a small money supply, we have a gross national product that is rising, and we have a relatively high interest rate.

Mr. MITCHELL. The rate pattern is partially a function of the foreign situation. Interest rates are not typical for this stage of a recession. Short-term interest rates are relatively high, and so are long-term interest rates relatively high compared to previous recessions.

Senator PROXMIRE. When the businessman goes to a bank, he wants to borrow money so he can expand his plant, put people to work, and so forth.

Mr. MITCHELL. Yes.

Senator PROXMIRE. When he goes and asks for the price of that money, it is high. As far as he is concerned, the situation is tight.

Mr. MITCHELL. The price of money may be high, but the situation is not tight. The banks would be delighted to lend to many people. They are looking for customers who want to borrow right now.

Senator PROXMIRE. The only way we can measure that objectively is what they are asking for money. Isn't that right?

Mr. MITCHELL. Yes, they are asking a high price for it.

Senator PROXMIRE. Let me just proceed to something else. I commend your attention to page 49 of the report of the Commission on Money and Credit where there is a very interesting discussion which, it seems to me, supports my position pretty well that velocity is simply the other side of money tightness.

Mr. MITCHELL. I think that the CMC report doesn't really handle velocity or turnover adequately.

Senator PROXMIRE. Then let me move on quickly.

Senator DOUGLAS. Before you abandon that, would you be willing to yield?

Senator PROXMIRE. Yes.

Senator DOUGLAS. Before you abandon that and turn to another subject, may I raise the point that there is a causal connection between a limitation of the money supply and high velocity, and that it operates through the interest rate.

If we restrict the supply of money so that there is a considerable amount of idle resources and idle labor, with the result that in the bidding for commercial loans there are high interest rates, do not these high interest rates speed up turnover by operating in two ways? First, businesses want to keep low inventories, so they cut their inventories as far as possible. Secondly, they reduce idle demand deposit balances in banks for which they are not paid interest. Thus the higher interest rates which come in consonance with the restriction of the money supply, in turn, as Senator Proxmire has said, increase velocity. Then this increase in velocity is used, as Senator Proxmire has pointed out, as a justification for the restriction in the money supply.

Mr. MITCHELL. Could I comment on this?

Senator DOUGLAS. Yes.

Mr. MITCHELL. This is the cyclical response of turnover to higher interest rates. As I was pointing out before, you have two factors affecting turnover and one is a secular one which depends on our financial mores, and the other is a cyclical one associated with interest rates. They both operate, but over the decade of the fifties, I think the institutional changes have been much more important.

Senator DOUGLAS. Suppose there is a secular increase in interest rates. May not that have an influence on the secular speedup?

Mr. MITCHELL. It would.

Senator DOUGLAS. On velocity?

Mr. MITCHELL. Once you have trained a corporation treasurer to keep his balances down, he will keep them low, even though the rates drop. He will have a little more edge on his appetite when the rates are higher. That is true.

Senator PROXMIRE. You conceded that the interest rates are high. You also agreed that the ratio between money supply and gross national product is as low as it has ever been. To me this may mean at least an element of tightness, as has been stressed very eloquently by Senator Douglas and Senator Clark. The fact is that we do have very, very heavy unemployment, nearly 8 percent seasonally adjusted. Our growth rate over the past few years has been very small. Isn't it logical on the basis of everything we have been talking about and everything we can see and everything our commonsense tells us that these high interest rates do have the effect of restraining business from borrowing? Therefore, don't they act as a brake on the economy at a time when we have many idle resources?

Mr. MITCHELL. Certainly higher interest rates restrain activity. That is true.

Senator PROXMIRE. Why is the Federal Reserve Board unable to adopt policies, in view of the fact that they have control of the supply of money, that will reduce the interest rates?

Mr. MITCHELL. As I was saying earlier, we have had a period of monetary ease. The effect on interest rates has been limited because of the international situation and the monetary ease is reflected not so much in the rates as it is in the easy position of the banks.

Senator PROXMIRE. The big difficulty I stumble over is that I feel very strongly that we should be very slow and very cautious and very careful about treading new economic paths. We have had magnificent success in this country. The one area where I feel the Government can act to stimulate the economy is in this monetary area. All of us agree that this is an area where we can properly act to stimulate. We see our economy idle. We see people out of work. We recognize the challenge of our European free countries as well as Russia. We are not moving ahead rapidly enough. I feel, therefore, that this is one area where we should be able to move ahead pragmatically and without any departure from our faith in our own system.

Mr. MITCHELL. Senator, the rate of gross national product in the first quarter of this year was about \$500 billion. The second quarter rate has been estimated at \$515 billion. And many people are predicting it will be \$540 billion by the end of the year. This is a pretty rapid upward surge in the economy. Another fact showing recovery is that the number of persons in wage and salary employment has increased in the past 4 months by something like 1.2 or 1.3 million. This is the largest increase in this particular series over a comparable time period that we had in the last three recessions.

Senator PROXMIRE. But the fact is that we still have nearly 8 percent unemployed and still have idle plant capacity. Because of the marvels of automation and technology we are getting higher productivity.

Mr. MITCHELL. We are getting a vigorous recovery at the moment and there is every reason to believe it is going to continue. And the monetary policy will play a role in this.

Senator PROXMIRE. Then I have just one other area which I will cover very quickly. Yesterday Frazar Wilde in discussing the report of the Commission on Money and Credit with the Joint Economic Committee recommended that the number of members of the Federal Reserve Board be reduced to five, that the Chairman be appointed so that his term coincides with that of the President of the United States, and that higher salaries be paid and more experienced people be appointed to the Federal Reserve Board. I wouldn't expect you to comment on all of these matters, particularly the latter perhaps. But I am wondering if you would agree that it is important to stress not only experience that is pertinent for appointees to the Federal Reserve Board, but also a broad appreciation of the overall interests of the economy.

Mr. MITCHELL. Yes, sir.

Senator PROXMIRE. Don't you feel there is some danger in stressing specific and particular pertinent experience of the appointee? By particular pertinent experience, I mean experience with banking and the kind of technical job that the Federal Reserve Board has to do.

Mr. MITCHELL. I think many people in the country are qualified to serve on the Federal Reserve Board. My experience in talking to people is that bankers generally come closer to understanding the problems of the Federal Reserve Board than most other people, but there are others that are qualified.

Senator PROXMIRE. That is the difficulty. They get a banker orientation. It is a wonderful orientation. There is nothing wrong with it. I was in banking in a modest way. It is one viewpoint that sometimes contradicts the interest of the public.

Mr. MITCHELL. I couldn't agree with you more. All I am saying is that there are more well-qualified people among bankers than among others. I don't think we should have more bankers on the Federal Reserve Board.

Senator PROXMIRE. Thank you. Thank you very much, Mr. Chairman.

The CHAIRMAN. Are there any further questions?

Senator LONG. I said a while ago that I didn't have any questions to ask. I have listened to these various theories. They have been all right on the high level. But I want to inquire as to the effect down in the grassroots.

As I understand, you say that there is a surplus of money now and that interest rates perhaps should be lowered.

Mr. MITCHELL. I say the typical response of the banking system to monetary ease on the part of the Federal Reserve System, when the demand for loans is low, is to expand their investments, and this has taken place.

Senator LONG. I have some knowledge of the small banks back in Missouri, and those banks have loan demands. Their loans now outstanding are maybe 50 or 60 percent of their assets. They are having trouble meeting their loan demands, especially in rural areas. So are many of our large city banks in the Middle West. How do you account for the statements that there is easy money now and money

rates are low when down at the grassroots we are having difficulty meeting our loan demands?

Mr. MITCHELL. Well, it is impossible to say what is true for every bank in the country. I think there are banks in the cattle-feeding areas, for example, that feel quite loaned up. But I don't think this is generally true. If you have to say something about the country as a whole, this would not be the correct statement.

Senator LONG. For banks down at the grassroots, wouldn't the fact that the costs of the supplies they buy, the salaries they pay, and their other expenses have materially increased the last year actually affect low-interest rates? Werent' low-interest rates a few years ago much cheaper with cheaper expenses? Banks are now required to charge a higher rate of interest to pay for these things.

Mr. MITCHELL. Banks ultimately will have to do what everybody else has had to do; they will have to find ways to cut their costs by one technique or another. There is a tremendous development taking place in banking now in the form of electronic accounting. This is going to make it possible for banks to operate cheaper eventually, and some of them already have made substantial savings.

Senator LONG. That doesn't take care of many of the smaller banks that exist in our banking system.

Mr. MITCHELL. That is true. They have a hard problem. Interest rates in the small communities are quite a bit higher usually than they are in the larger centers.

Senator LONG. You don't have figures to indicate whether money is tighter in the rural areas than generally over the country?

Mr. MITCHELL. No, sir.

Senator LONG. That is all.

The CHAIRMAN. Anything further?

Senator PROXMIER. I do apologize. I have one more question, which is very important for me.

On page 64 of the report of the Commission on Money and Credit, there is the following recommendation:

The Commission recommends the continued use of open-market operations as the normal or usual instrument of general monetary policy. Instead of relying on a "bills-only" policy, the Federal Reserve should be willing, when domestic or international conditions warrant, to influence directly the structure as well as the level of interest rates in pursuit of countercyclical monetary policies and should deal in securities of varied maturities. This recommendation does not mean a return to a pegged structure of prices and yields for government securities. And the normal use of open market operations in bills to carry out technical and seasonal changes in bank reserves is appropriate.

I ask this question because to me it is one of the really crucial issues in this whole area. You say that you disagree with some of the recommendations, and that you agree with others. I wonder if you can tell us how you feel about this.

Mr. MITCHELL. On the question of bills only, that is an unduly doctrinaire position, and I would have no particular difficulty in endorsing the statement of CMC. I think it is easier to operate in bills only, but I think you may be more effective in operating across the board.

The CHAIRMAN. Thank you.

The committee will now go into executive session.

(Whereupon, at 11 a.m., the committee went into executive session.)